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N.2792

No. 13800

United States Court of Appeals for the Ninth Circuit.

ROBERT DONALD ROWLAND,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Appeal from the United States District Court for the Southern District of California Central Division.

FILED
JUN - 1 1953
PAUL P. O'BRIEN

Phillips & Van Orden Co., 870 Brannan Street, San Francisco, Calif.—5-29-53

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

NAMES AND ADDRESSES OF ATTORNEYS

For Appellant:

J. B. TIETZ,
257 S. Spring St.,
Los Angeles 12, Calif.

For Appellee:

WALTER S. BINNS,
United States Attorney;

RAY H. KINNISON, and
MANUEL L. REAL,
Assistants U. S. Attorney,
600 Federal Bldg.,
Los Angeles 12, Calif.

In the United States District Court in and for the Southern District of California, Central Division

No. 22530-CD

September, 1952, Grand Jury

UNITED STATES OF AMERICA,

Plaintiff,

vs.

ROBERT DONALD ROWLAND,

Defendant.

INDICTMENT

[U.S.C., Title 50, App., Sec. 462—Selective Service Act, 1948]

The grand jury charges:

Defendant Robert Donald Rowland, a male person within the class made subject to selective service under the Selective Service Act of 1948, registered as required by said act and the regulations promulgated thereunder and thereafter became a registrant of Local Board No. 113, said board being then and there duly created and acting, under the Selective Service System established by said act, in Los Angeles County, California, in the Central Division of the Southern District of California; pursuant to said act and the regulations promulgated thereunder, the defendant was classified in Class I-A-O and was notified of said classification and a notice and order by said board was duly given to him to

report for induction into the armed forces of the United States of America on July 28, 1952, in Los Angeles County, California, in the division and district aforesaid; and at said time and place the defendant did knowingly fail and neglect to perform a duty required of him under said act and the regulations promulgated thereunder in that he then and there knowingly failed and refused to be inducted into the armed forces of the United States as so notified and ordered to do.

A True Bill.

/s/ LAURENCE L. ROGERS,
Foreman.

/s/ WALTER S. BINNS,
United States Attorney.

ADM:AH.

[Endorsed]: Filed October 15, 1952. [2*]

[Title of District Court and Cause.]

MINUTES OF THE COURT—OCT. 27, 1952

(Arraignment and Plea)

Present: The Hon. Wm. C. Mathes,
District Judge.

Proceedings:

Defendant is arraigned and pleads not guilty as charged in the Indictment.

It is Ordered that this cause is set for jury trial Nov. 24, 1952, 1:30 p.m.

*Page numbering appearing at foot of page of original Certified Transcript of Record.

It Is Ordered that this cause is continued to Nov. 10, 1952, 11 a.m., for hearing on motion to dismiss.

EDMUND L. SMITH,
Clerk;

By /s/ S. W. STACEY,
Deputy Clerk. [3]

[Title of District Court and Cause.]

MOTION TO DISMISS

The defendant moves the indictment be dismissed on the ground the indictment is based on the Selective Service Act of 1948, whereas the offense, if any, was committed on July 28, 1952, a date more than one year after the adoption of Public Law 51, 87th Congress (Universal Military Training and Service Act), approved June 19, 1951.

Dated November 4, 1952.

ROBERT DONALD
ROWLAND,

By /s/ EDWIN H. HIBER,
Attorney for Defendant.

Affidavit of Service by Mail attached.

[Endorsed]: Filed November 6, 1952. [4]

[Title of District Court and Cause.]

ORDER DENYING MOTION TO DISMISS

This matter came on for hearing on the 24th day of November, 1952, on Motion to Dismiss the Indictment herein, and the Court being fully advised in the matter,

It Is Ordered that said Motion to Dismiss the Indictment herein be, and the same is hereby denied, and

It Is Further Ordered that this case be, and the same is hereby continued for trial to December 1, 1952, at 1:30 p.m.

Dated November 24th, 1952.

/s/ WM. C. MATHES,
United States District Judge.

[Endorsed]: Filed November 26, 1952. [6]

[Title of District Court and Cause.]

WAIVER OF TRIAL BY JURY AND WAIVER OF SPECIAL FINDINGS OF FACT

[Rule 23(a) and (c) F.R.C.P.]

The undersigned defendant hereby waives the right to a trial by jury and requests the court to try all charges against him in this cause without a jury.

The undersigned defendant further waives the right to request any special findings of fact as pro-

vided by Rule 23(c) of the Federal Rules of Criminal Procedure.

December 1, 1952.

/s/ ROBERT DONALD ROWLAND,
Defendant.

The undersigned counsel represents that prior to the signing of the foregoing waiver, the defendant above named was fully advised as to the rights of an accused under the Constitution and laws of the United States, including the right to a trial by jury and the right to request special findings in a case tried without a jury; and further represents that, in his opinion, the above waiver by the defendant of trial by jury and special findings is voluntarily and understandingly made.

December 1, 1952.

/s/ J. B. TIETZ,
Attorney for Defendant.

The United States Attorney hereby consents that the case be tried without a jury, and waives the right to request any special findings of fact as provided by Rule 23(c) of the Federal Rules of Criminal Procedure.

December 1, 1952.

/s/ WALTER S. BINNS,
United States Attorney;

By /s/ MANUEL L. REAL,
Assistant U. S. Attorney.

December 1, 1952.

/s/ WM. C. MATHES,
United States District Judge.

[Form Cr. 23]
[Mathes, J.]

[Endorsed]: Filed December 1, 1952. [7]

[Title of District Court and Cause.]

MINUTES OF THE COURT—FEB. 9, 1953

Present: The Hon. Wm. C. Mathes,
District Judge.

Proceedings: For further proceedings on trial.

Attorney Tietz moves for a continuance. Said motion is denied.

Both sides rest. Counsel argue.

Court Finds defendant guilty as charged and orders cause referred to Prob. Officer for investigation and report and continued to Feb. 24, 1953, 10 a.m. for sentence; defendant to remain on present bond.

EDMUND L. SMITH,
Clerk;

By /s/ P. D. HOOSER,
Deputy Clerk. [8]

[Title of District Court and Cause.]

MOTION IN ARREST OF JUDGMENT

Now comes Robert Donald Rowland, defendant in the above case, and asks that the verdict of guilty heretofore returned against him be arrested and no judgment and sentence be imposed thereon for the following reasons:

I.

That the indictment upon which the defendant was tried and convicted does not state facts sufficient to constitute a crime against the United States.

II.

Defendant relies on:

A. The points and authorities in the file, heretofore submitted, and on

B. The fact the Grand Jury itself has changed the content of its selective service indictments to conform to the objections raised by defendant.

/s/ J. B. TIETZ,
Attorney for Defendant. [9]

[Title of District Court and Cause.]

MOTION FOR NEW TRIAL

The defendant moves the court to grant him a new trial for the following reasons:

1. The court erred in denying defendant's motion for acquittal made at the conclusion of the evidence.

2. The verdict is contrary to the weight of the evidence.

3. The verdict is not supported by substantial evidence.

Dated at Los Angeles February 25, 1953.

/s/ J. B. TIETZ,
Attorney for Defendant. [10]

[Title of District Court and Cause.]

RECEIPT OF MOTIONS AND WAIVERS

Receipt is acknowledged of Motion in Arrest of Judgment and Motion for New Trial in the above case.

Time for service of Motion is waived and plaintiff consents, subject to approval of the Court, that said motions may be heard on March 3, 1953.

WALTER S. BINNS,
United States Attorney;

RAY H. KINNISON,
Assistant U. S. Attorney, Chief of Criminal Division;

/s/ MANUEL L. REAL,
Assistant U. S. Attorney,
Attorneys for Plaintiff.

[Endorsed]: Filed February 25, 1953. [11]

[Title of District Court and Cause.]

MINUTES OF THE COURT—MARCH 2, 1953

Present: The Hon. Wm. C. Mathes,

District Judge.

Proceedings: For sentence, on finding of guilty.

It is stipulated that motion for new trial and motion in arrest of judgment be heard at this time instead of on March 3, 1953.

Attorney Tietz argues in support of motions.

Court Denies motion in arrest of judgment and denies motion for new trial.

Court Sentences defendant to four years imprisonment for offense charged in Indictment, and orders bail of defendant exonerated.

EDMUND L. SMITH,
Clerk;
By /s/ P. D. HOOSER,
Deputy Clerk. [12]

United States District Court for the Southern District of California, Central Division

No. 22530-Cr. Indictment

[1 Count—for Violation of 50 U.S.C. § 462]

UNITED STATES OF AMERICA,

vs.

ROBERT DONALD ROWLAND.

JUDGMENT AND COMMITMENT

On this 2nd day of March, 1953, came the attorney for the government and the defendant appeared in person and with his attorney, J. B. Tietz, Esquire.

It Is Adjudged that the defendant has been convicted upon his plea of not guilty and a finding of guilty of the offense of having on July 28, 1952, in Los Angeles County, California, knowingly failed and neglected to perform a duty required of him under the Selective Service Act of 1948 and the regulations promulgated thereunder in that he then and there knowingly failed and neglected to report for induction into the armed forces of the United States as so notified and ordered to do, as charged in the Indictment; and the court having asked the defendant whether he has anything to say why judgment should not be pronounced, and no sufficient cause to the contrary being shown or appearing to the Court,

It Is Adjudged that the defendant is guilty as charged and convicted.

It Is Adjudged that the defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of four years in an institution to be selected by the Attorney General of the United States or his authorized representative for the offense charged in the indictment.

It Is Adjudged that the bail of the defendant be exonerated.

It Is Ordered that the Clerk deliver a certified copy of this judgment and commitment to the United States Marshal or other qualified officer and

that the copy serve as the commitment of the defendant.

/s/ WM. C. MATHES,
United States District Judge.

EDMUND L. SMITH,
Clerk;

By /s/ P. D. HOOSER,
Deputy Clerk.

[Endorsed]: Filed March 2, 1953. [13]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Appellant, Robert Donald Rowland, has been residing at 129 N. Greenwood Ave., Montebello, California.

Appellant's attorney, J. B. Tietz, maintains his office at 534 Douglas Bldg., 257 S. Spring Street, Los Angeles 12, Calif.

The offense was failing to submit to induction, U.S.C., Title 50 App., Sec. 462—Selective Service Act, 1948.

On February 9, 1953, the court found the defendant guilty [jury trial having been waived] and on March 2, 1953, the court sentenced the appellant to four years confinement in an institution to be selected by the Attorney General, and is presently in the Los Angeles County Jail.

I, J. B. Tietz, appellant's attorney, be authoribed

by him do hereby appeal to the United States Court of Appeals for the Ninth Circuit from the above-stated judgment.

/s/ J. B. TIETZ,
Attorney for Appellant.

Receipt of copy acknowledged.
[Endorsed]: Filed March 4, 1953. [14]

In the United States District Court, Southern District of California, Central Division

No. 22530-WM-Crim.

Honorable William C. Mathes, Judge, Presiding.

UNITED STATES OF AMERICA,
Plaintiff,

vs.

ROBERT DONALD ROWLAND,
Defendant.

REPORTER'S TRANSCRIPT
OF PROCEEDINGS

Appearances:

For the Plaintiff:
WALTER S. BINNS,
United States Attorney, by
JAMES K. MITSUMORI,
Asst. United States Attorney.

For the Defendant:
EDWIN H. HIBER, ESQ.,
Appointed by the Court.

Monday, October 27, 1952—11:00 A.M.

(Case called by the clerk.)

The Court: Is Robert Donald Rowland your full, true name?

The Defendant: Yes, sir. [2*]

* * *

Mr. Clerk, will you ascertain what is now the plea of the defendant to the charge in the indictment?

The Clerk: What is your plea to the charge in the indictment?

The Defendant: May I ask a question first?

The Clerk: Yes.

The Defendant: I would like to know do I have to be present in court to move that the case be dismissed, or can that be handled on paper, written?

The Court: You should be present at all stages of the [6] proceedings. You may sign a waiver of the right to be present if you so desire. The clerk will furnish your counsel with a form, and you need not be present at the hearing of any motion to dismiss unless you so desire, provided, of course, you sign the waiver.

The Defendant: Where can I get that?

The Court: The clerk will furnish your counsel with a form of waiver.

You have a form of waiver pursuant to Rule 43, Mr. Clerk? Hand it to counsel.

Are you ready to plead at this time, Mr. Rowland?

The Defendant: Yes.

*Page numbering appearing at top of page of original Reporter's Transcript of Record.

The Court: How do you plead to the indictment? Are you guilty or not guilty?

The Defendant: Not guilty.

The Court: The clerk will enter a plea of "not guilty" on your behalf. [7]

* * *

The Court: Mr. Rowland, I have before me a waiver of trial by jury and waiver of special findings of fact pursuant to Rule 23. It appears to be signed by you and by Mr. Tietz as your attorney; is that correct?

Defendant Rowland: Yes, sir.

The Court: Is it your desire to waive your constitutional right of trial by jury and have your case tried by the court without a jury?

Defendant Rowland: Yes, sir.

The Court: The case involves a question of law, does it not, Mr. Tietz?

Mr. Tietz: Yes, sir.

The Court: In your opinion, Mr. Tietz is the defendant's waiver voluntarily and understandingly made?

Mr. Tietz: Yes, your Honor.

The Court: Very well, I will approve the waiver.

You are instructed, Mr. Rowland, to return to Judge Tolin's courtroom on this floor of this building on **January 5th next at 1:30.**

Mr. Real: May it please the court, I think you set that for Thursday. I believe it was this Thursday.

The Court: Oh, I am sorry. Yes. It is set for 1:30. Thank you.

You will return Thursday afternoon of this week, December 4th, at 1:30, Mr. Rowland. Do you understand the time? [29]

Defendant Rowland: To this court?

The Court: To this courtroom. Do you understand the time?

Defendantant Rowland: Yes.

The Court: Next Thursday afternoon at 1:30.

(Intermission for other court proceedings.)

The Court: Mr. Tietz, in case No. 22,530 is there any question about the exhaustion of the administrative remedies in the Rowland case?

Mr. Tietz: There could be, your Honor, yes. He took no appeal. He did report but refused to submit to induction. So if the matter is raised as a stumbling block to his presenting his defense, your Honor might very well decide that he is foreclosed.

If there is any possibility, through co-operation of the United States Attorneys' office, in having the local board giving that chance, we would certainly welcome it. In the past I have not been able to secure that, except when there is an outright violation such as having made his request within the 10 days period and he has not gotten it.

The Court: In two cases this afternoon they were continued to permit further administrative proceedings, and it occurred to me that that same problem might be involved in the Rowland case. I am not suggesting whether there is any merit or lack of merit in the possibility, or not. [30]

Mr. Teitz: We would welcome it. And I would

ask the court—and I am pleased that the court has on its own motion brought the matter up, placed the matter back in the calendar and given the defendant that opportunity, if the United States Attorney will intercede.

The Court: This case is set for Thursday afternoon at 1:30 now.

Mr. Tietz: Yes, your Honor.

The Court: Does the Government have any views on that?

Mr. Edward J. Skelly (Assistant U. S. Attorney): No, your Honor. Mr. Real, who is handling that, your Honor——

The Court: Has the defendant Rowland left?

Mr. Tietz: I am certain, because I have been out in the hall and he is not there.

The Court: Perhaps you gentlemen might consider it and we will take it up Thursday afternoon at 1:30. Other cases have been put over to permit that opportunity. I may be in error, but it just occurred to me from the Rowland file that that probably might be lurking there.

Mr. Tietz: This is the first time we have been accorded that opportunity by any United States District Judge, I might say, or any of my clients, and I appreciate that.

The Court: Very well, we will take it up Thursday at 1:30, gentlemen.

(Whereupon, a recess was taken until Thursday, December 4, 1952, at 1:30 o'clock [31] p.m.)

Thursday, December 4, 1952, 1:30 P.M.

(Appearances as last heretofore noted.)

(Case called by the clerk.)

Mr. Real: Ready for the Government, your Honor.

Mr. Tietz: I appear for the defendant, your Honor.

Mr. Real: The defendant is present in court, your Honor.

The Court: Are you ready? How long will it take, gentlemen?

Mr. Tietz: Your Honor, this was a matter in which the suggestion was made that a continuance of 30 days might be advisable for the purpose of securing a reprocessing, a partial reprocessing by the Selective Service system due to the fact that this defendant had never had a personal appearance nor an appeal on his claim that he was a conscientious objector. His claim was recognized to an extent he was given a I-A-O, but only to a limited degree.

I am informed today, a few minutes ago, that Maj. Keeley, Area Co-Ordinator, has said "no" to the Government's suggestion that there be this partial reprocessing.

My request to the court is this: That it still be continued for some period so that an effort can be made, partly by me and partly by the Government, and this is what I would represent to Maj. Keeley: That there is always a possibility that the court in sentencing this defendant, if he should be [32]

unable to win the verdict of acquittal, might do what a judge of this court did on September 22nd, and that is make a probationary order with the usual conditions, but with this unusual one, that the defendant not be required to obey any Selective Service law unless—now, your Honor, this was not——

The Court: You do not need to proceed any further. I would never make a probationary order that anyone not be required to obey any law.

Mr. Tietz: Now, your Honor, may I finish my sentence?

The Court: Yes.

Mr. Tietz: And it may throw a different light on the whole situation—unless the Selective Service system give the boy the appeal, and if the Selective Service system gives the boy an appeal, which he never had, and an order is thereafter made that he report for and submit to induction, that he be required then to obey that order.

So that, Judge Yankwich, by that order, which I may state was an order that was made in many, many cases during World War II—I have a list of the numbers, the cases and the judges of 50—I stopped then because my purpose was served and I did not go back farther—50 probationary orders, all of which I consider genuine probationary orders. I checked those myself. * * * [33]

So what I am hoping might eventuate, I say I am going to represent to Maj. Keeley and the others involved, might possibly be your Honor's order, is that we have a great deal of precedent from this court, all eight judges sitting on the bench

during World War II up to the surrender of Germany, because after that I think there was a dropping off.

So that it is entirely possible that when Selective Service is informed of what just happened recently they will say the boy should have his appeal and we will give him the appeal. That is all we request. My request is that there be a continuance of some sort for the purpose of permitting me to go to Selective Service with that request.

Mr. Real: May I be heard, your Honor?

The Court: Yes.

Mr. Real: It is the feeling of our office that, first of all, we have no guarantee that even if we could procure the requisite signature from the Attorney General, we have no guarantee of any possible kind that this thing would not be repeated again even after appeals and hearings by officers other than the Local Board. Our indictment is based on the fact that this defendant was properly ordered to induction in the armed forces and that he refused to submit to induction.

The Court: Do you oppose the motion for a continuance? Is that what you are saying? [34]

Mr. Real: Yes, for the continuance of 30 days for the purpose of reprocessing, the Government does oppose the motion, your Honor.

Mr. Tietz: The time need not be 30 days, your Honor. Inside of a week or two I could get the matter determined by the Selective Service, deter-

mined as to whether or not they will give the boy the appeal.

The Court: There has been a waiver of trial by jury here?

Mr. Tietz: If there has not, there will be one.

The Court: There is one in the file. Does the Government oppose?

Mr. Real: I beg your pardon?

The Court: Does the Government oppose a continuance?

Mr. Real: It opposes the continuance for 30 days, yes, your Honor, for the purposes stated by Mr. Tietz. Yes.

The Court: How much time will you need, Mr. Tietz?

Mr. Tietz: Oh, I would think two weeks would be sufficient, because Maj. Keeley may wish to refer to Sacramento. He may not want to take the full responsibility himself. I can state there has been at least one instance where he wanted to do something to help out a boy I represented and it was overruled later. So I think two weeks will be sufficient.

The Court: Does the Government oppose that?

Mr. Real: Your Honor, from my talk with Maj. Keeley [35] this morning he seems to be of the opinion that there was nothing that could be done so far as the Selective Service Board was concerned; that as far as they were concerned this defendant was processed through their processes, all the processes that they could do under the circumstances. He made no request.

The Court: Mr. Tietz just wants one more chance, I suppose, is that it?

Mr. Tietz: Yes, your Honor. If for no other reason than when we do come into court, if we must come into court, I won't be blocked from presenting the defense that he has not exhausted his administrative remedies.

The Court: Is it your contention that he has not exhausted his administrative remedies?

Mr. Tietz: That statement was made Monday, and frankly, when I was aware that the Government might present that to block me from presenting a defense—now, I think he has got a good defense, even as it stands now, and if I should not be able to present that defense solely because he has not exhausted his administrative remedies, it would be certainly very sad for the defendant.

The Court: Has he exhausted his administrative remedy? Is there a contention he has not? I made the suggestion possibly he had not, but I think I was in error from the fact that the Government contends, at least. [36]

Mr. Teitz: My understanding is that he never had an appeal; is that correct? And his answer, which may or may not be determinative of exhaustion, is that he went down to the local board office within the 10 days period to do the next step and the clerk said: "There is nothing more you can do." And if I get by the argument that he has not exhausted his administrative remedies, I am presenting the argument on frustration, which may or may not appeal to your Honor. If it does not

appeal to your Honor, this boy's defense can't be made out.

The Court: Cannot be made out?

Mr. Tietz: If your Honor follows me and says he has not exhausted his administrative remedies because he did not take an appeal.

Mr. Real: If it please the court, from the evidence——

The Court: Does the Government contend that this defendant has not exhausted his administrative remedies?

Mr. Real: I contend that he has exhausted his administrative remedies, because the regulation and the notice of classification is quite clear, in precise language, that any appeal that is to be taken is to be taken within 10 days after classification and must be in writing, and that was not done in this case. So he has gone as far as he can go legally in exhausting his administrative remedies.

The Court: Assuming he was ordered to report for [37] induction, did not that mark the exhaustion of the administrative remedies, Mr. Tietz?

Mr. Tietz: I was going to rely on that Gibson decision of the Supreme Court that I would be permitted to present my defense. But when on Monday this matter was brought up and I thought that the court would take a different view and would think that because he had not availed himself of the opportunity for an appeal, which would give the Selective Service a chance to remedy its own mistake, and that I therefore might be blocked, I jumped at the court's very kind offer that he

have this chance to exhaust his administrative remedy. But if the position the Government has now stated is that he has exhausted his administrative remedy, if that is going to be their position at trial, then my reason has been cut out for another hearing and I have remaining only the reason that it might be better for all concerned, including the court's time, that this boy does get an appeal. Because a boy that is given a I-A-O has a good chance of getting a I-O from the appeal board, because he has been submitted by the local board as sincere and having genuine scruples.

Mr. Real: If the court please, this is not the question in this case. This case is quite clear under the Cox decision that the only decision to be made is whether or not he was ordered under a valid order to be inducted and whether he refused to obey that order. [38]

The Court: Mr. Tietz is raising a technical question, as I understand it, rather than a legal one, aren't you?

Mr. Tietz: Yes, now I am in that position.

The Court: You just want some time to see if the Selective Service system wishes to do anything more about it, is that it?

Mr. Tietz: Right.

The Court: Not as a matter of right but as a matter of grace.

Mr. Tietz: No. It has become that, yes.

The Court: In view of the Government's position that the administrative remedies have been exhausted legally.

Mr. Tietz: Yes.

The Court: How long will that take, two weeks?

Mr. Tietz: Two weeks would be sufficient time.

The Court: Is there any prejudice to the Government?

Mr. Real: There will be no prejudice to the Government. We oppose that sort of a motion, for the purpose of information, only on policy.

The Court: How long will it take to try this case, Mr. Tietz?

Mr. Tietz: An hour and a half or two hours at most.

Mr. Real: That is our estimate, your Honor.

The Court: Let us continue it, then, to December 22nd, for Tuesday or Wednesday, just prior to Christmas. December [39] 22nd, at 1:30, Monday afternoon, and try the case probably Tuesday, Tuesday morning or Tuesday afternoon.

Mr. Tietz: And the defendant appears at 1:30 on the 22nd?

The Court: Yes. Is that an agreeable time to both sides?

Mr. Real: It is agreeable to the Government, your Honor.

The Court: Very well. Mr. Rowland, you will return to this courtroom on December 22nd next, at 1:30 in the afternoon. Do you understand the time?

The Defendant: Yes, sir.

(Whereupon a continuance was taken until Monday, December 22, 1952, at 1:30 o'clock p.m). [40]

Monday, December 22, 1952, 1:30 P.M.

The Clerk: No. 27 on the calendar: 22,530-Criminal, United States of America vs. Robert Donald Rowland. Mr. Manuel Real for the Government, Mr. Tietz for the defendant. Is the defendant present, Mr. Tietz?

Mr. Tietz: He is.

The Clerk: And are you the defendant?

Defendant Rowland: Yes.

The Court: Did you hear anything from the state director in this matter?

Mr. Tietz: The answer is "no," your Honor.

The Court: Very well. How long will it take to try the case?

Mr. Tietz: Perhaps two hours.

Mr. Real: About half a day, your Honor.

The Court: Is tomorrow morning agreeable at 10:00 o'clock?

Mr. Tietz: Yes, your Honor.

The Court: Very well, I will continue the case for trial. It is non-jury, is it not?

Mr. Tietz: That is right.

The Court: Until tomorrow morning, December 23, at 10:00 o'clock. You are instructed to return at that time to this courtroom, Mr. Rowland. Do you understand the time and place? [41]

The Defendant: Yes, sir.

The Court: Very well.

(Whereupon a recess was had until the following day, Tuesday, December 23, 1952, at 10:00 o'clock a.m.) [42]

Tuesday, December 23, 1952, 10:00 A.M

(Counsel present as last heretofore noted.)

The Clerk: Case No. 22,530, United States vs. Robert Donald Rowland.

Mr. Real: Ready for the Government, your Honor.

The Court: Is the defendant present?

Mr. Tietz: Yes, your Honor.

The Court: You may proceed.

Mr. Real: Your Honor, at this time the Government would like to waive its opening statement in view of the trial memo filed with your Honor in this case.

The Court: You may. The jury waiver has been approved, has it?

Mr. Real: Yes, your Honor.

The Court: The defendant still wishes, I take it, to waive the right of trial by jury and proceed?

Mr. Tietz: Yes. That has been his desire always.

The Court: Very well, you may proceed.

Mr. Real: Call Maj. Keeley, please.

ELIAS M. KEELEY

called as a witness by the plaintiff, being first sworn, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: Elias M. Keeley, K-e-e-l-e-y. [43]

Direct Examination

By Mr. Real:

Q. Maj. Keeley, what is your occupation?

A. I am a Major in the United States Army, as-

(Testimony of Elias M. Keeley.)

signed to Selective Service, and have charge and known as the District Co-Ordinator for Selective Service System.

Q. As part of your assignment do you have legal custody and control of the Selective Service files of registrants for local boards in your area?

A. I have the general supervision of all files in Southern California.

Q. Do you know the defendant Robert Donald Rowland?

A. I know him by sight and I have talked with him.

Q. Do you see him in court today?

A. Yes.

Q. Will you point him out, please?

A. He is sitting alongside of Mr. Tietz.

Q. Is the defendant Robert Donald Rowland a registrant, to your knowledge, of Local Board 113?

A. We have a Robert Donald Rowland that is a registrant of Board 113, yes.

Mr. Real: May it be stipulated that this Robert Donald Rowland who is the defendant here in court is the same Robert Donald Rowland who is a registrant of Local Board 113?

Mr. Tietz: Yes. [44]

Q. (By Mr. Real): You have brought with you today an original of his Selective Service file?

A. I have.

Mr. Real: Will the clerk place Government's Exhibit 1 for identification before the witness?

Q. Government's Exhibit 1 for identification now

(Testimony of Elias M. Keeley.)

before you, Maj. Keeley, that is the original Selective Service file of Robert Donald Rowland?

A. That is correct.

Q. And is it the normal course of Local Board 113's business to keep that record, and that record is kept in the normal course of Local Board 113's business? A. It is.

Mr. Real: At this time, your Honor, we would like to introduce into evidence Government's Exhibit 1 for identification.

Mr. Tietz: All right for identification, your Honor. And I might state——

The Court: It is offered into evidence now.

Mr. Tietz: We have no objection to the introduction of the file, the complete file, into evidence, except for the following item—and I think we could save time by going into that matter now.

The Court: Very well.

Mr. Tietz: Page 27—these pagination marks have been [45] made by the Clerk, I believe, and not the normal numbers of any of the sheets. They are found at the bottom of each of the sheets and circled. Pages 27 and 29 are duplicate pages.

Our objection to both is that it is a document that is dated August the 1st, 1952, long after the processing of the defendant. but that would not be too material. Our chief objection is that it contains a misstatement. It says that he is a member of Jehovah's Witnesses, and I think that will be conceded, and therefore I ask the Government to stipu-

(Testimony of Elias M. Keeley.)

late that these two sheets not be included in the file under "D."

The Court: The defendant is not a member of Jehovah's Witnesses?

Mr. Tietz: That is correct: There is no dispute about that.

The Court: Does the Government so stipulate?

Mr. Real: So stipulated, your Honor.

Mr. Tietz: And then the defendant will object to the admission into evidence of sheet 51 which bears the Local Board's stamp July 31st, for the same reason; and our actual non-technical reason is that the Reverend Page, who is referred to in this memorandum that the clerk made and inserted, herself, in the file——

The Court: The clerk of the local board? [46]

Mr. Tietz: Yes. It bears her signature and it is a mere typing of a memo on a sheet of paper, and it will confuse the record for this reason: This Rev. Page is not the minister of this defendant's church, represents a different fellowship, a non-pacifist fellowship, and the statement made here by the clerk ascribing certain beliefs to him are not the beliefs of this defendant, and therefore would confuse the record.

So I ask the Government to stipulate that sheet No. 51 not be made part of the record.

Mr. Real: So stipulated, your Honor.

The Court: As I understand the stipulation, it is that pages 27, 29 and 51 of Exhibit 1 for identification, the pages so marked with those numerals in-

(Testimony of Elias M. Keeley.)

closed in circles at the foot of the pages designated, not be received into evidence.

Mr. Real: May it please the Court, page 27, one of those may be deleted, but we ask that one of them be in, with the possible interlineation and the correction as to the Jehovah's Witness, and that the "Church of Christ" be inserted in it. That is part of his record, your Honor.

The Court: We cannot change the Selective Service records. You may stipulate that they are incorrect to that extent.

Mr. Real: I will stipulate to that extent that they are incorrect, but not that they will be deleted from the file, your Honor.

The Court: Is there any objection to pages 27 and 29 [47] in view of that stipulation?

Mr. Tietz: No, the defendant has no objection.

The Court: What about page marked "51," then?

Mr. Real: We will stipulate that it may be deleted, your Honor.

The Court: Very well. Then Exhibit 1 for identification is now received into evidence, with the exception of the page thereof marked "51" which Mr. Tietz has heretofore described, Mr. Tietz referring to "Rev. Elwood A. Page." That is your objection, Mr. Tietz?

Mr. Tietz: Yes, your Honor.

The Court: Very well.

Mr. Real: May I have Exhibit 1-A for identification?

(Testimony of Elias M. Keeley.)

The Court: Mr. Clerk, you will mark the sheet designated "51" as Exhibit 1-A for identification.

The Clerk: Your Honor, there is already another file marked 1-A. There is a photostatic copy to substitute.

The Court: What is Exhibit 1-A?

Mr. Real: 1-A is a photostatic copy, your Honor. I am about to make a stipulation.

The Court: Let it be Exhibit 2, photostatic copy of the file.

Mr. Real: That is correct, your Honor.

The Court: And the deleted page 51 from Exhibit 1 will be marked 1-A for identification. The Exhibit 2 is a photo-copy [48] of the complete file?

Mr. Real: That is correct, your Honor.

The Court: Does it contain a photostatic copy of——

Mr. Real: The particular pages deleted?

The Court: No, the page 51, which is the only page deleted.

Mr. Real: That is correct, your Honor.

The Court: And let us now mark it Exhibit 1-A for identification.

Very well, Mr. Clerk, will you remove this page marked "51" from Exhibit 2 for identification and mark that page Exhibit 2-A for identification?

The Clerk: Yes, your Honor.

Mr. Real: May it please the Court, may it be stipulated that Exhibit 2, Government's Exhibit 2 for identification, is a photostatic copy of the Selec-

(Testimony of Elias M. Keeley.)

tive Service file of Robert Donald Rowland marked Government's Exhibit 1-A in evidence?

The Court: 1 in evidence.

Mr. Real: I am sorry, your Honor. No. 1 in evidence, and that it be introduced into evidence in lieu of the original Selective Service file of Robert Donald Rowland marked Government's Exhibit 1, and that Government's Exhibit 1 be withdrawn from evidence at this time and returned to this witness, your Honor.

Mr. Tietz: The defendant will so stipulate. [49]

The Court: Very well, so ordered pursuant to stipulation. Exhibit 2 for identification is received into evidence. Exhibits 1 and 1-A for identification may be withdrawn and returned to the witness.

Mr. Real: Cross-examine.

The Court: Have you any cross-examination of this witness?

Mr. Tietz: No cross-examination.

The Court: You may step down, Maj. Keeley.

Mr. Real: The Government will rest its case at this time, your Honor.

Mr. Tietz: The defendant would like to make a motion to acquit. The defendant has two grounds for his motion. One is very substantial and the other is a matter of first impression, and it might well be that, on a technical basis, it alone is sufficient.

The defendant's first ground is that there must be a basis for every Selective Service classification, although the defendant would be willing to concede that perhaps there need not be—I will invite the

Court's attention to the various parts of the exhibit as I make my argument on this point.

The defendant would perhaps be willing to concede that the Selective Service system may give registrant a I-A classification without any basis of fact because of the wording of the definition of "I-A" that places the burden on [50] the registrant to satisfy the board that he is entitled to or has a status of some other classification. But that, fortunately, does not enter into this case.

While there have been a number of decisions that I-A classifications have been given without any basis of fact, a number of acquitals, fortunately we do not have as difficult a problem as that here. We have what I think is a comparatively easy problem.

We have a situation where the local board has stamped this defendant a truthful, sincere and honest registrant who is a conscientious objector. He professes to be one. They say he is one. And, of course, according to the Supreme Court decisions interpreting the intent of Congress, their decisions of fact are final; and in the absence of some arbitrariness, in the absence of some denial of due process, the court cannot go behind it. We are not asking the court to go behind their decision that he is a genuine conscientious objector.

We point out to the court that what the board has attempted to do is this: It has attempted to say—your scruples with respect to the conscientious objection that you profess to have and which Congress says you are entitled to have and are to be respected, that those scruples do not go as far as you say they

go, and we therefore are drawing a line—a line that you do not draw. We draw the line at I-A-O. We say [51] that, on the facts before us, presented by you or gathered by us and reduced to writing, which is what the regulations require, on the facts before us—put in other words, the file—we see that you are willing, really, as a matter of fact, to do non-combatant work. You say you are not, but the facts show otherwise.

Now, if there is something in the file—and this is a challenge to the Government—if there is something in the file that they could put their finger on and say: This is the basis of fact for the board's decision, then my point is gone.

I have gone through the file. I do not see it. Possibly some ecclesiastical reference, some scriptural quotation he has given might be tortured into some line-drawing that he does not make. I do not think so.

I have gone over it carefully, and while I do not profess to know the scriptures that well, I do not think there is anything and I say to the Government, "point out any one fact."

Now, the reason why I wanted page 51 out of the record—I am now making an argument I think I will be allowed to on this point. Page 51 is the memo made by a clerk of the board of a conversation she had with a minister of a Church of Christ.

It is common knowledge that there are six branches, six different fellowships of the Church of Christ. One of those [52] six is known as a pacifist fellowship. There are 200 congregation in that fel-

lowship. That is the fellowship that this defendant belongs to. And it so happens that Rev. Page was and he is an old friend of the boy's grandmother, which, if necessary, will come out in the evidence if we are required to put on our defense evidence.

I am anticipating, but I want the court to understand why I am making this argument. It will save time later. That when Rev. Page is quoted as saying that the I-O, the complete conscientious objector position, is not the position taught by his church, that that is not binding on this defendant and was made long after, made a year and a half after the classification was made. So that could not have been the basis for the board's classification. But in order to keep it out of the record, that there could be a scintilla of evidence, even, I might say, by taking what was said a year and a half later, I wanted it out at that time, but I am sure within the stipulation by the Government it should go out.

So I say this: The Government must show something. It would be too much of a burden on the court to find something, and I tried to find something. The Government has studied the file, and Maj. Keeley has had more experience. Let them point out one thing on which the court can say that is a basis of fact for this decision.

There have been quite a number of decisions, [53] district court decisions, it is true, on this point. Unfortunately, they are all district court decisions and none of them have as yet been reported, but I have slip sheets on all of them, the ones that I will mention. I would like to read just one paragraph from

one of them to give the court the reasoning of the other district judges who have been faced with this problem. I will read from the case of United States of America vs. James J. Relyea, the opinion of the court March 18, 1952. It is the Northern District of Ohio, Eastern Division, Judge McNamee. And on page 2 of his opinion he says:

"I think it would have been more difficult for the court to find the act of the board was without any basis in fact if the board has classified this man in I-A rather than I-A-O. They accepted the defendant's profession of sincere and conscientious objection on the religious grounds as being truthful, but they attempted—and in my opinion, without any basis in fact—to assert that, while he was sincere and conscientious, that sincerity and conscientiousness extended only to his aggressive participation in military service and that he was not sincere in his statement that he was opposed to war and participation to war in all its forms."

And that is precisely the situation that we have here. [54] I am satisfied, your Honor, that that alone is enough to justify the court in granting the motion.

Now, I have another matter which I wish to present to the court that, as I said, is a matter of first impression in that no court has yet been called on to rule on it. I think it is something which one of these Selective Service defendants should bring up, and the court could very well use it as its sole basis for granting the motion.

I will read from the Selective Service regulation.

I am reading from Section 1604.56. And while this is the page which was promulgated in the Federal Register, I suppose, September 24th, it is dated September 28, 1951. I assure the court that this particular regulation was in effect in exactly these words at all times during the processing of this defendant. I mention that because these regulations change quite frequently, as the court might know. I have two volumes of obsolete ones. They are just as thick as the main one.

This regulation says this——

The Court: What is the number of it?

Mr. Tietz: 1604.56, from 32 C.F.R It reads as follows:

"Each local board shall elect a chairman and a secretary. A majority of the members of the local board shall constitute a quorum for the [55] transaction of business. A majority of the members present at any meeting at which a quorum is present shall decide any question or classification. Every member present, unless disqualified, shall vote on every question or classification. In case of a tie vote on any question or classification, the board shall postpone action on the question or classification until it can be decided by a majority vote."

And then it goes on with some matters which do not concern us.

I will invite the court's attention to what is now paginated as page 11, which gives the fact page or page (8) of Selective Service form No. 100, classification questionnaire, and it is called: "Minutes of Actions by Local Board and Appeal Board."

We see after every action of the board, such as the second lines: "Nov. 15, 1950 I-A-O," and we also see on August 13, 1952, when they declared him a delinquent, we see two things, a numerical vote and a set of initials. And I say "a set," I mean one set for each line. The vote in one instance says "3-0" with reference to "I-A-O" classification, and there is one set of initials "C.K.H."

On the other action it was "2-0," so it says, and the initials are "E.G."

Now, my argument is this: The Supreme Court in Old vs. [56] Smith has declared that when an individual signs a document with his initials he is merely abbreviating his name. So that my next step here is, you have a written name, and my point, therefore, is, we have a conflict between the writing and numerals, and the broad rule of law, I say, governs, that writing takes precedence over numerals.

Now, it may well be that actually there was a quorum at each of these meetings. It may well be that each of the board members did as he was required to do and voted. But my point is the record does not show that and we, I say, have made out a prima facie case that there was no quorum present and that a majority of the members or a quorum did not vote for these particular classifications.

Possibly the plaintiff can come in and show that that is not so, but until that is shown, unless there is an offer to show that, I say that there is no quorum present.

For these two grounds the defendant is entitled to a dismissal, should be sent back to the Selective

Service system where, this time, he can get what Congress has assured him he should have—a determination of his claim, meaning a complete determination with the whole procedure.

When the court goes through the file in trying to determine it, I say, in determining whether or not there is a basis of fact, the court will be struck, I believe, by one of the sheets that I invite the court's attention to now. [57]

The Court: Is there anything in the record to indicate that these initials are initials of members of the local board?

Mr. Tietz: Yes, your Honor. My argument on that point would be this: We look at the initials and we see they end up with an "H." We also see the handwriting. We look at the order to report for induction and we see that it is signed, as it can be, by a member of the board named Horn. We look at the handwriting and we see it is the same handwriting.

The Court: I noticed on page 11 where three members purportedly voted to classify the defendant as I-A-O, that there is only apparently the initials of one person.

Mr. Tietz: Yes. That is what I am unhappy about. That is what I think shows, at least prima facie, that there was not a quorum. The evil that the regulation that I read obviously tries to avoid is this: The defects of the minds are such that some board members, since there are thousands of board members—that some board member might, as we say in the vernacular, go off his rocker and might

come down to the board office sometime and, all by himself, classify everybody I-A, and a quorum must be present. He might out of malice. And so General Hershey, in the name of the President, promulgated this regulation, and I say it is a good regulation, that there must be a quorum present and a majority must vote for every classification. [58]

The Court: Would you read that regulation again? That is 32 C.F.R. 1605.54.

Mr. Tietz: ".56," your Honor.

The Court: "56."

Mr. Tietz: In italicized printing it is entitled: "Organization and meetings." That is all, and I will read every word and the punctuation, your Honor.

"Each local board shall elect a chairman and a secretary. A majority of the members of the local board shall constitute a quorum for the transaction of business. A majority of the members present at any meeting at which a quorum is present shall decide any question or classification. Every member present, unless disqualified, shall vote on every question or classification. Every member present, unless disqualified, shall vote on every question or classification. In case of a tie vote on any question or classification, the board shall postpone action on the question or classification until it can be decided by a majority vote. If any member is absent so long as to hamper the work of the local board, the chairman of the local board shall recommend to the State Director of Selective Service that such member be removed and a new member appointed."

I think we can stipulate that this qualification,

that [59] proviso about disqualification, refers only to when a board member is a relative or some such —Maj. Keeley is very familiar with that—so that it does not enter into this picture here.

Now, there is one sheet that I would like your Honor to read before arriving at a decision as to whether or not there is a basis of fact. That is a letter that the young man wrote to the local board. He wrote two in fact, and I find this one at pages 53 and 54, but the other one is shorter. It is at 25, page 25, and very revealing.

The Court: Does that complete your argument?

Mr. Tietz: Yes, your Honor.

Mr. Real: May it please the Court, answering Mr. Tietz's argument, first, on classification, it would be just calling your attention to Regulation 1622.10.

"Class I-A: Available for military service. In Class 1-A shall be placed every registrant who has failed to establish to the satisfaction of the local board, subject to appeal hereinafter provided, that he is eligible for classification in another class."

It is the Government's position that a registrant starts out under this regulation with a I-A classification and upon him the duty is placed to show that he is entitled to some other classification. [60]

Mr. Tietz asks us to show some basis in fact for the classification of the local board. I call your Honor's attention to the page paginated 14 and to the paragraph "(e)":

"Describe carefully the creed or official state-

ments of said religious sect or organization in relationship to participation in war."

Under that sentence the defendant and the registrant at that time placed these quotations from the Bible:

"it is wrong to kill (Romans 13:9), it is wrong to fight with carnal weapons (2 Corinthians 10:3-5; Ephesians 6:12; Matthew 26:52) it is wrong to participate in carnal warfare (John 18:36)."

This registrant started out with the classification of I-A presumptively. From there we go to what this particular statement, which is the only statement that we have, since it is quoted also on page 12, the answer to sentence 2, in essentially the same language.

It is the Government's position that this is just a matter of interpretation of the Bible and that the local board could reasonably have given this registrant the classification that it gave him, "I-A-O," and "I-A-O" classification is a classification given to men who are opposed to participation in combat service but who are not opposed to participation as a non-combatant. [61]

There is no evidence in the file any place of this particular registrant that he could show at that time that he was objecting to non-combatant service, other than the signature of his name under paragraph (B) Claim for Exemption Series I on page 12.

The Court: Page 12?

Mr. Real: That is correct, your Honor.

The Court: He makes that statement under oath, doesn't he?

Mr. Real: No, your Honor. This is not a form under oath This is merely a form that is submitted to the board. It is taken home or sent to the registrant and is not under oath. There is no evidence to this statement.

Then he goes on to strengthen that by his quotations from the Bible. It is the Government's contention that those quotations do not show an objection to participation as a non-combatant in service.

The Court: Well, is it the Government's position that the registrant must cite Biblical authority for the dictates of his conscience?

Mr. Real: It is not the contention that he must cite Biblical authority; but it is the contention of the Government that he must support his signature or his opposition to war so that the local board may have something on which it is to base its classification if he is to be classified a complete [62] conscientious objector. That was not done in this case.

Further, answering the second question that Mr. Tietz raised——

The Court: Before you do that, suppose a registrant comes in and says: I believe that. That is my creed. I believe it. Those are the dictates of my conscience.

Where did I learn it? I learned it in Sunday School when I was 12 years old. It has always been my creed. That is the only religious training I have had.

Mr. Real: I think, your Honor, that the cases on the classification as to I-O or as to a conscientious objector and the law in that respect is that if a per-

son is entitled to a classification of I-O, not on the basis of his own philosophical convictions, but on the basis of religious training and beliefs——

The Court: He says that is what I was taught in Sunday School.

Mr. Real: Then I think, your Honor, it is a question of fact as to whether the local board believes him or not, and that question is not before this court.

The Court: The point here, as I understand it, is this: He says that is what I was taught and that is what I believe. Now, the statute says "Religious training and experience." What does "experience" mean?

Mr. Real: Well, "experience" to me, your Honor —I [63] do not know what the statute means in itself—"experience" to me is the sum total of the life of an individual.

The Court: He says: By reason of religious training—I am sorry—not "experience," "religious training and belief."

Mr. Real: The question of religious training may be shown by documentation. The question of belief is a question that would not be shown by documentation, your Honor. I think it is a question of either believing a registrant or not believing what he says.

The Court: The registrant must have religious training, I take it, which teaches him these things, plus his own conscientious objection from that teaching.

Mr. Real: That is correct, your Honor. And, as a basis, the defendant places in the file these answers

to these questions: That it is wrong to kill; it is wrong to fight with carnal weapons. Taking it just from general knowledge, the question of the interpretation of the Bible, I think each recognized religion has a different interpretation of what the words "It is wrong to kill" mean. Some religions believe it is wrong to kill lest you kill in self-defense. Other religions believe it is wrong to kill even in self-defense. So I think it is a question of this particular registrant.

If he has not shown that to the satisfaction of the local board and they classify him, that classification is final [64] under the Cox case.

The Court: The point made here, as I understand it, is that if this registrant believes at all, there is no rational basis for believing him halfway and not believing him all the way.

Mr. Real: The question of his belief, from the evidence in the file, would lead reasonable men to believe that this particular registrant was opposed to combatant service but not to non-combatant service, and that is the classification he was given.

The Court: Do you intend by that to suggest that the board believed him as to the combatant service but not as to the non-combatant?

Mr. Real: It would appear from the classification that they gave him that that is exactly what they did.

The Court: You may proceed to the next point.

Mr. Real: Along those lines, I think, your Honor, once that that has been established and that

the local board has made the classification, it is final, within the ruling of the Cox case.

As to Mr. Tietz's second point as to regulation 1604.56, I think that I have only just one or two things to direct to that. First of all, that Mr. Tietz has forgotten, evidently, the presumption of regularity that goes to official procedures; and that there is nothing in this regulation that shows [65] or that requires that every member of the board initial or sign any part of the findings of that particular meeting. It says only that they must participate, and that in participating they must vote unless disqualified. I think that the record itself stands on that.

I think that the entry of "3-0," since there are three members in a local board, shows that there was a quorum there sufficiently enough, and that the quorum voted and the vote was 3 to nothing, and the entry was made by somebody whose initials are "C.R.H." and it would take an expert, I think, to determine whether "C.R.H." was the same person who signed the order of induction.

And I also think that, since when a board consists of three men, that a vote of "2-0," would show that there was a quorum present, since a quorum is only a majority of the board, and that two votes were cast, and the result of the vote was 2 to nothing, and that that vote was initialed on entry by a person whose initials are "E.G."

I think in consideration of that, we just stand on the presumption of regularity in these proceedings, and on that point, the definition of the Cox

case that the record is the summation of the classification and that that is what is to be considered upon the review by this court.

Mr. Tietz: Might I have two or three minutes, your Honor?

The Court: You may. [66]

Mr. Tietz: I will make comment on the second point first. The defendant concedes that there is a presumption of regularity for all official acts. The defendant contends that the presumption has been met by the prima facie case the record presents, and that the burden then is on the Government to go forward if it can.

With respect to another portion of that point, the Government states that it was a three-man board. I believe there was no evidence to that effect. And while we might be inclined to concede, because it is not known to me that it was not a three-man board, it is a fact that there are five-man boards, and the regulation—I haven't the place open, but I think the Government will stipulate that there are five-man boards. So that in the face of the statute record, we do not know if this was only a three-man board.

But I would like to go on to the other matter which does require more than some technical consideration.

The Government did not read another answer that this defendant gave in the same questionnaire, merely referred to it.

On page 12, wherein he answered the second question of the second series, the second series being

entitled: "Religious Training and Beliefs" and the second question being:

"Describe the nature of your belief which is the basis of your claim made in Series I above, [67] and state whether or not your belief in a supreme being involves duties which to you are superior to those arising from any human relation."

The defendant wrote out, and I admit it is a little difficult to read, but I think we should understand that fully because I believe it completely answers the question that was made, the argument made was that he did not say he was opposed to non-combatant service, and I say this does answer that squarely. He says:

"I believe that it is wrong to kill."

And I believe it is a Romans quotation he gives. He goes on to say:

"that it is wrong to fight with carnal weapons."

He gives a Corinthian reference. Then he quotes Ephesians and Matthew. And then he goes on to say:

"And participate in carnal warfare."

Quoting John; and then he gives the expression which I think makes it doubly certain:

"Since these are the duties of Military Service I can't join them."

He goes on to say:

"I also believe it is my duty to meet with the Church of Christ on the first day of the week."

I think that can be interpreted to mean that any duty of military service would interfere with his religious duties, [68] but I do not rely too much

on that. I rely on the others, that wearing the uniform is something he can't do, because he is joining with the others. And I think if the court were to look up the Second Corinthian reference, I think the court would find a very interesting reason that he gives there, because Second Corinthians, if I remember correctly, reads something like this: "I shall not be united in any manner with unbelievers." And that is another reason which many pacifists give for not wanting to be in uniform. It may not be a strong reason to you or me, but to a man who asserts it for religious reasons it may be as strong as the other.

He goes on finishing this question:

"I believe that I should obey the Lord rather than man."

In any event, it seems to me that it is torturing this file, when you take all the professions he has made, to say that he has not made the profession that he cannot participate in any way in warfare.

The Court: He has made that declaration; there is no question about that, is there?

The question here, Mr. Tietz, is whether any local board or whether this local board acted within the bounds of reason under all the circumstances, isn't it?

Mr. Tietz: I say the dilemma the local board is in, and the local board could solve the dilemma very easily—— [69]

The Court: You and I might decide these differently. These problems of conscience are very delicate problems. Someone must decide them.

Mr. Tietz: Correct.

The Court: And if the board had classified him in I-O, I do not suppose anyone would contend that there was no reasonable basis for that classification.

Now, by the same token, can anyone say that the classification I-A-O was not within the bounds of reason?

Mr. Tietz: I do, and I do for these reasons: If they had said to him we give you a I-O, then I would be in an almost untenable position, because by giving him a I-O they would be saying: We do not believe your professions, and that right has been given them by Congress.

The Court: You mean I-A?

Mr. Tietz: I-A, yes. But when they say: We do believe you, but when they give him a I-A-O they believe him, they stamp him as a conscientious objector. They try to draw a line, and maybe there is a line. Some of these files do show that there is a line, but this file does not show there is a line. And if it can be pointed out where the line is, then I would say that my argument just doesn't apply. The Government's argument, the real argument, is that they did not believe him. They did believe him, but they attempted to do an illegal thing. [70]

I will put it this way, your Honor: The local board and the whole Selective Service system under the intent of Congress, under the Supreme Court decisions, has the right to be wrong, as any one of us has a right to be wrong in our judgments. But it has not the right to be illegal, and when it makes a decision that has no basis of fact, when it draws a line that he does not draw, that none of

his evidence draws, it is illegal; it is beyond its jurisdiction.

Very often a young man comes in to a board and says in effect: I am a I-O, and then he presents evidence which shows he is not a I-O; he is only a I-A-O.

If this board did the right thing, this board would have said: He makes out a prima facie case. There is a lawyer on the board. What we will do is do what he could do, ask for a personal appearance hearing. We will call him in and then, by quizzing him, find out if there is some place where his scruples stop and that he could, without violating his conscience, wear a uniform, and do some type of non-combatant work. And then when the board summarized that hearing, there would be in the files a basis to support it. There is no basis here.

The Court: Is there anything in the Christian teachings—this registrant is a Christian—is there anything in Christian teaching that you know of, that is, Christian teaching as taught by Christ and the Disciples, which tells anyone [71] not to associate with sinners?

Mr. Tietz: I do not want to appear to evade the court's question, but I take this flat position: Even if the New Testament was universally understood to mean, to just use one illustration of what I understand the Catholic position is, that there is such a thing as a just war, I suppose every Christian——

The Court: Just leave that "war" out of it.

This is non-combatant service. A man is not participating in the acts of war.

Mr. Tietz: I have discussed these matters with many conscientious objectors, and particularly among a pacifist class of conscientious objectors, and I have found that they give many reasons which were entirely satisfactory to them and to very learned ministers, and they go like these. They quote the scriptures. I quoted on, Second Corinthians:

"I shall not be united with unbelievers."

Another one: "Ye shall not take oaths." The fact it is a practice, and the fact that in the Army a man must take an oath—he cannot do like a defendant would do here if he was called to the stand, his will affirm.

In other words, there are scriptural bases which, to the court and me, might not seem substantial enough to bar the court or me from engaging in such an enterprise.

The Court: I am not attempting to pass upon that, Mr. [72] Tietz, or upon the conscientious objections of any person. The board here has that problem.

My question is directed to this: In human experience a Christian who would say he is conscientiously opposed to having any contact with sinners would be the exception rather than the rule, wouldn't he?

Mr. Tietz: Oh, yes. I would say just roughly——

The Court: So the board, acting as it did, they say in effect: We believe this young man is con-

scientious in his opposition to participating in war, but they do not believe that his conscientious scruples carry him to the point where his is conscientiously opposed to participation in non-combatant service.

Now, it might have been easier, it might have been even a sounder basis to reach the contrary result. In other words, there might be a better argument, if you please, to put him in the classification I-O than I-A-O, but that is not even our problem, is it? Our problem is whether there is any rational basis, whether it is within the bounds of reason on this record to put him in I-A-O.

Mr. Tietz: Not so much rational basis. I would differ with the court.

The Court: Rational basis in fact, yes. And I take it that they proceed from some premise of fact, and that is a very broad statement to make, isn't it? [73]

Mr. Tietz: There is no question, and the board felt, the board unquestionably felt that this young man could be placed in I-A-O without violating his scruples. They felt that way. But they must have—I keep repeating myself—a basis of fact for it. And if Mr. Real can point out where there is a basis of fact, then I will concede it.

Let me give an illustration of an actual case, a case up now in the Supreme Court for other reasons. This case is reported in the last advance sheet of the Federal. It is the Head case that I argued before the Tenth Circuit, and I argued that there was no basis of fact. In that case the United

States Attorney, neither in the trial court nor in the Court of Appeals, could present to the court a basis of fact, but the learned Chief Judge Phillips who was assigned to write the opinion went through the file and he came up—now, that is the next point and I am in a very difficult position to try to show now that something in that file is not true. He came up with what was the basis of fact, and by relating it to the court the court will see what I mean about a basis of fact.

In the special form 150 the defendant, answering the question: "On whom do you rely for your religious guidance?" instead of saying "Jesus" or "the Bible" or whatever this defendant did, he claimed a man, a certain minister of his fellowship. The FBI in their investigation—because [74] that defendant had the appellate procedure—the FBI interviewed him and then the FBI agent made an honest, very natural misstatement of that man's position, quoted him as saying: "Yes, I would help a wounded soldier. Yes, I would care for the wounded." And the FBI man, in my opinion, wholly honestly, not conceiving that an individual willing to do that on a battlefield would balk at wearing a uniform—to the FBI man that was of no consequence—said he teaches the I-A-O position. Therefore Judge Phillips said that he relied on that man for his guidance and that man teaches the I-A-O position, and therefore this is a basis of fact, and that is so ruled on this opinion which has just come up.

I am taking it from other points. I have affidavits

it was not so and other points in the case. But if Mr. Real can point out something like that in this case, not merely say that the board has a right—it has, but it has to base it on a fact. It cannot make it on a whim; it cannot make it on a fine-spun philosophical reason that people cannot interpret the Bible this way. If there is some basis of fact, one iota, one scintilla of fact, then my whole argument will fall, but I say there is not.

The Court: These must be very difficult questions for any draft board or any other group of people to pass upon—questions of conscience.

As I view it, there is not necessarily any disbelief [75] that this record shows of the defendant in the finding of the draft board. They might have felt that this did not disclose an understanding of what non-combatant service is. This is a difficult chore. I think most of us can be glad we do not have it. We would not want the chore of compelling any man to violate the deep-seated dictates of his conscience.

I have no doubt the officials who were charged with the enforcement of this law believe as I do, that a man's conscience is the oracle of God. They do not want to compel him to do anything that would disregard that oracle. I am confident Congress did not wish to in enacting the law.

Someone must make findings of fact on these matters. The Supreme Court has said that when those findings are made by the proper officials they are like other findings of fact under our system of

justice if there is a reasonable basis for them, even though reasonable men might differ. If the fact found is within the bounds of reason, the known facts upon the record and upon the evidence, then it is not for this court or any court to substitute its judgment for the judgment of the board, the law having imposed upon the board the duty of making that finding. If its finding is within the bounds of reason, it must be sustained.

I am under the duty of sustaining the finding of the local board. The defendant is found guilty as charged.

Mr. Tietz: But, your Honor, I have not rested. I [76] am merely arguing a motion to acquit.

The Court: I am sorry. The motion for judgment of acquittal is denied.

Mr. Tietz: I will call the defendant.

The Clerk: Any objection to swearing?

The Defendant: Yes.

ROBERT DONALD ROWLAND

the defendant herein, called as a witness in his own behalf, having duly affirmed to tell the truth, the whole truth, and nothing but the truth, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: Robert Donald Rowland.

Direct Examination

By Mr. Tietz:

Q. What church do you belong to?

A. The Church of Christ.

(Testimony of Robert Donald Rowland)

Q. When did you join the Church of Christ?

A. I was baptized May the 8th, 1948.

Q. Do you mean that by baptism you performed the act of joining or that is a formal entrance?

A. Yes, that is when I was added to the church.

Q. How long have you been a member? How long have you been associated with the Church of Christ?

A. I have attended the Church of Christ all my life. [77]

Q. Now, page 11 of the exhibit (2) shows that on November 21, 1950, four days after the board apparently met and classified you I-A-O, Form 110, which is a postcard, was sent to you. Do you remember getting a notice or postcard telling you what classification was given you? A. Yes.

Q. What did you do when you got it?

A. Cut it down and put it in my wallet.

Q. You did what?

A. I cut it down and put it in my wallet.

Q. You mean there was a portion of that postcard that had a dotted line with instructions to cut it out and put it in your wallet and carry it with you, is that it? What else did you do? Did you notice what classification was on it?

A. Yes.

Q. What was it? A. "I-A-O."

Q. Is that what you asked for?

A. No.

Q. Did you do anything about it?

A. Yes, I went over to the draft board.

(Testimony of Robert Donald Rowland)

Q. What did you do there?

Mr. Real: If it please the court, I will object to this line of questioning as irrelevant and immaterial to this particular proceeding; that under the Cox case the only [78] question here is as to whether he received a notice of induction and as to whether he refused to submit pursuant to that notice of induction. That is the only question before this court, your Honor. So far as any classification and the legality of that notice of induction, it is a question of law for your Honor to decide from the records.

Mr. Tietz: Might I be heard briefly, your Honor?

The Court: Do you offer it as relevant to the issue of specific intent?

Mr. Tietz: No, your Honor. We offer it on this basis: That we are laying a groundwork for a denial of due process, and under a long line of cases, including court of appeals decisions after the Cox case, it is recognized that, as I put it before, although the board can be wrong in its judgment, it cannot be illegal in its acts, so that if I can show a denial of due process, even though there may be a basis of fact—and that is what a number of the recent cases have said—even though there is a basis of fact, if there is a denial of due process, it is the right of every citizen to show that it is still there.

The Court: If that is the purpose, the objection is overruled. You may answer.

(Testimony of Robert Donald Rowland)

Mr. Tietz: May the reporter read the question, please?

(Last portion of record read by the reporter.)

A. I talked to the clerk. [79]

Q. And what was the conversation?

A. Well, I asked the clerk concerning the classification. I said that was not the classification that I filed for, that I deserved. She told me that inasmuch as the draft board had classified me that, that they would not change their decision.

Q. When you went down there you went for what purpose?

A. To see about having the classification changed.

Q. And did you notice on the postcard, in very fine print, what the printers call six-point type——

Mr. Real: I will object, your Honor, on the grounds that this is leading the witness.

The Court. Overruled.

Q. (By Mr. Tietz): ——that on this postcard in the smallest type there, in what the printers call six-point type, there was something about personal appearance or something about appeal? Did you have a personal appearance?

A. I considered that a personal appearance.

Q. What did you consider as a personal appearance? A. When I appeared at the board.

Q. I see. Did you speak to her about an appeal?

A. Yes.

Q. What was the conversation on that?

(Testimony of Robert Donald Rowland)

A. Well, as I already said before, she said as I had already been classified in I-A-O, that the board wouldn't [80] change their decision.

Q. Did you ask her if there was anything you could do to get them to change the decision?

A. Yes.

Q. And what did she say?

A. She said there wasn't.

Mr. Tietz: You may cross-examine.

Cross-Examination

By Mr. Real:

Q. Mr. Rowland, how much schooling have you had?

A. I went to junior college about two and one-half years after getting out of high school.

Q. You had average grades in junior college, is that correct? A. Yes, about average.

Q. Average or better than average?

A. About average.

Q. And you read and write the English language adequately; you consider yourself——

A. Well, enough for my own purposes.

Q. For your own purposes. You said, Mr. Rowland, that you read the notice of classification that you were sent by the local board, is that correct?

A. Yes, after I cut it down and put it in my wallet.

Q. Did you read the whole card? [81]

A. Yes.

(Testimony of Robert Donald Rowland)

O. And the notice of the right to appeal?

A. Yes.

Q. And in that notice—did you read it very carefully? This is very important to you, isn't it, this decision as to what the local board made?

A. Yes.

Q. So that you were to avail yourself of everything that the local board was supposed to give you, is that correct? A. That is right.

Q. On that card did you notice it says: "Appeal from classification by the local board must be made within 10 days after the mailing of this card by filing a written notice of appeal with the local board"? Did you read that? A. No.

Q. Did you tell me you read this notice of appeal? A. Yes.

Q. Did you read that within the same 10-day period you may file a written request for personal appearance? A. No.

Q. But you read this notice? A. Yes.

Q. "If this is done, the time in which you may appeal is extended 10 days from the date of mailing the new notice of classification after such personal appearance." Did you [82] read that?

A. I got the classification. It is something like two years ago and I don't remember what was on it, word for word.

Mr. Real: May it please the court, if the clerk may mark Selective Service form 110 as Government's 3 for identification.

The Court: It may be so marked.

(Testimony of Robert Donald Rowland)

The Clerk: Government's Exhibit 3 for identification.

Q. (By Mr. Real): I place before you Government's Exhibit 3 for identification, Mr. Rowland, and ask you to read that. Now, I will ask you is Government's Exhibit 3 for identification the exact copy of the Notice of Classification, without your classification or your name and serial number? In other words, that is the notice that you received, the same type of notice?

A. It stated the same general things on it.

Q. The same general things?

A. I don't know that it was an exact copy.

Mr. Real: Can it be stipulated, your Honor, that this Form 110 is the same type copy that was sent?

Mr. Tietz: The defendant will stipulate that it is so similar that there is no material difference in whatever you have there. I have not seen it. I have seen only one, but they are so similar that there is no material difference.

The Court: Please show the exhibit to [83] counsel Mr. Real, always show the exhibits to counsel before you show them to the witness.

Mr. Real: I am sorry, your Honor.

Q. Mr. Rowland, when you received that card you were apprised at that time that you were entitled to a personal appearance before the local board and then, as I say, if it denied any of your claims at that time, that you were entitled to an appeal, is that correct?

A. I didn't understand the question.

(Testimony of Robert Donald Rowland)

Q. I say, when you received the notice, Form 110, Government's 3 for identification, you knew at that time that you were entitled to a personal appearance before the local board and that if the local board refused the classification which you wished, that you were entitled to an appeal, is that correct?

A. I knew about a personal appearance, yes.

Q. You found out from that card, is that correct? A. No.

Q. How did you find out?

A. I knew it before.

Q. And what did you consider a personal appearance before the local board?

A. When I appeared at the board.

Q. And did you submit anything in writing to the local board concerning your personal appearance or an appeal [84] therefrom? A. No.

Mr. Real: Thank you.

Mr. Tietz: There is just one question, your Honor.

Redirect Examination

By Mr. Tietz:

Q. Do you recall about when you went down to the local board and had this conversation with the clerk? A. It was within a few days.

Q. That is all—a few days after you received that notice of classification? A. Yes, sir.

Mr. Tietz: That is all.

The Court: How long?

Mr. Tietz: I beg pardon?

(Testimony of Robert Donald Rowland)

The Court: How long after you had registered was it that you went down to the local board to make that appearance?

The Witness: I don't remember. It was shortly after I got this card, within a week or so.

The Court: When did you receive the card, about?

The Witness: Just a minute. I got it (witness producing wallet)—it was mailed November 21, 1950. I imagine I received it a day or two after that.

The Court: You had been registered over a year at that time, had you not, under the Selective Service System? [85]

The Witness: I registered November 4, 1949.

The Court: That would make it a little over a year?

The Witness: Yes.

The Court: I want to be sure I understand you. Is it your testimony that all during this time when you were a registrant, up to the time you went down to make a personal appearance before the board, that you did not know anything about a registrant's right to appeal a classification?

The Witness: I knew that I had the right to a personal appearance before the board. I considered that was an appeal.

The Court: Did you read this "Special Form for Conscientious Objector" prior to the time you filed it on November 6, 1950?

The Witness: Which form is that?

The Court: Please place before the witness, Mr.

(Testimony of Robert Donald Rowland)

Clerk, Exhibit 2 opened to page marked 12. Toward the center of the page is some printed matter. Did you read that at the time you filled in the form?

The Witness: Where it says "Instructions," yes, I read it.

The Court: Read it right now, will you?

The Witness: To myself or out loud?

The Court: Read it out loud.

The Witness: "A registrant who claims to be a conscientious objector shall offer information [86] in substantiation of his claim on this special form, which when filed shall become a part of his Classification Questionnaire (SSS Form No. 100).

"The questions in Series II through V in this form are intended to obtain evidence of the genuineness of the claim made in Series I, and the answers given by the registrant shall be for the information of only the officials duly authorized under the regulations to examine them.

"In the case of any registrant who claims to be a conscientious objector, the local board shall proceed in the prescribed manner to determine his proper classification. The procedure for appeal from a decision of the local board on a claim of conscientious objection is provided for in the Selective Service Regulations."

The Court: Did you read that last sentence which you last read there at the time you filled in that form?

The Witness: Yes.

The Court: Didn't that convey to you that there

(Testimony of Robert Donald Rowland.)

was a right of appeal from an adverse ruling on your claim?

The Witness: Yes. I considered my appearance at the draft board as an appeal.

The Court: Anything further?

Mr. Tietz: I have some other witnesses, your Honor. [87] Will you step down, Donald?

The Court: You may call your next witness.

Mr. Tietz: The defendant will call Rev. Page.

Mr. Real: If it please the court, before we go into this may Maj. Keeley be excused now as a witness in this case, your Honor?

Mr. Tietz: We have no objection.

The Court: Very well, you may be excused.

ELWOOD A. PAGE

called as a witness by the defendant, having affirmed to tell the truth, the whole truth and nothing but the truth, was examined and testified as follows:

The Clerk: State your name, please.

The Witness: Elwood A. Page.

Direct Examination

By Mr. Tietz:

Q. Mr. Page, I am going to place before you a portion of the exhibit entitled—one sheet, but it is entitled pages 49 and 50, which apparently is a card, the front and the back side, a double card.

The Court: You refer to pages 49 and 50 which are one sheet?

Mr. Tietz: Yes, your Honor.

(Testimony of Elwood A. Page.)

The Court: Of Exhibit 2?

Mr. Tietz: Yes, your Honor [88]

Q. Will you tell us if you are the minister of the defendant's congregation? A. I am not.

Q. Are you an old friend of the family, of his grandmother? A. Yes.

Q. Is that the reason for you coming to the local board and endeavoring to help this young man?

A. That is true.

Q. Is it a fact that you belong to a different fellowship of the Church of Christ than he does?

Mr. Real: May it please the court, I will object to this line of questioning. I see no relevancy to to the issues in this case.

Mr. Tietz: That is an exhibit——

The Court: Overruled.

Mr. Tietz: ——and I wish to have the record show how Rev. Page came into the picture and that he is not the minister of this defendant, and that this defendant is not bound by what may be on that card.

The Court: I think the objection is well taken but I will overrule it. He may explain the exhibit.

Mr. Tietz: That is my sole purpose from this witness.

The Witness: I would like to explain the situation as such. Each congregation of the Church of Christ is a [89] sovereignty of its own, and as to considering the phraseology of "fellowship" I am not the minister of the congregation or the group that meets that this boy is a member of under the

(Testimony of Elwood A. Page.)

eldership there. Each congregation is a sovereignty of its own, ruled by the eldership of the congregation.

Q. Am I right in believing that there are a half a dozen divisions of the Church of Christ, each numbering hundreds of congregation, and that the division or fellowship—whichever term you prefer using—that you belong to has different attitudes toward a number of things such as baptism and towards Sunday Schools and so on than the fellowship that this defendant belongs to?

A. On doctrinal points there are some phases of difference; yes, sir.

Q. And your card evidences some of those differences that his fellowship does not; I believe the card mentioned Sunday Schools and a number of things such as that? A. That is true.

Mr. Tietz: That is all, thank you. You may cross-examine.

The Court: Any questions?

Mr. Real: No cross-examination.

The Court: You may step down, Mr. Page.

Mr. Tietz: Mr. Dallas Stone, please. [90]

DALLAS E. STONE

called as a witness by the defendant, having first affirmed to tell the truth, the whole truth and nothing but the truth, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: Dallas E. Stone.

(Testimony of Dallas E. Stone.)

Direct Examination

By Mr. Tietz:

Q. Mr. Stone, you are acquainted with the defendant? A. I am.

Q. For how long have you known him?

A. Oh, I don't know just how old he is, but since he has been about a year and a half old, I believe.

Q. Do you occupy any position, have any title in the Church of Christ congregation of which he is a member?

A. Yes, I am called the leader there.

Mr. Real: I renew my objections at this time, your Honor, as to this witness. It is irrelevant to any point in this case.

The Court: No pending question, Mr. Real.

Q. (By Mr. Tietz): Because of the fact you have known him since he was an infant and any other facts that you may wish to give us, have you the means of knowing his reputation among his associates for truthfulness?

A. Yes, I know his reputation very well, [91] being associated with him since he was just a baby, you might say. He has always had a reputation of being honest, sincere and upright, and I have never known him into any mischief of any kind.

Q. How often have you seen him during the last 18 or 19 years?

A. Well, I would see him once a week and then perhaps once during the middle of the week. For

(Testimony of Dallas E. Stone.)

instance, every Sunday, and then in between times once or twice a week.

Q. And you know his associates and his friends? A. Yes, sir.

Mr. Tietz: Thank you very much. You may cross-examine.

Mr. Real: No cross-examination, your Honor.

The Court: You may step down.

Mr. Tietz: Mr. John Sharp, please.

JOHN H. SHARP

called as a witness by the defendant, having first affirmed to tell the truth, the whole truth and nothing but the truth, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: John H. Sharp.

Direct Examination

By Mr. Tietz:

Q. Do you occupy a position in the congregation of which this defendant is a member?

A. Yes, sir. [92]

Q. And has it a name or a title?

A. I am one of the leaders. In addition to that, why, I am secretary-treasurer of the congregation.

Q. How long have you known this defendant?

A. I have known him for better than 19 years.

Q. How well have you been able to get acquainted with him?

A. Well, I have been regularly associated with

(Testimony of John H. Sharp.)

him and his family ever since that time. The greater part of the time we have lived within one block of each other, and my association has been close and constant.

Q. Do you have the means of knowing his reputation for truthfulness? A. Yes, sir.

Q. What is his reputation?

A. His reputation, so far as I know, is perfect.

Q. Well, if it was otherwise, would you know?

A. I believe I would.

Mr. Tietz: That is all.

Mr. Real: No cross-examination, your Honor.

The Court: You may step down, Mr. Sharp.

Mr. Tietz: Step down, please. Mr. Ervin Waters.

J. ERVIN WATERS

called as a witness by the defendant, having first affirmed to tell the truth, the whole truth and nothing but the truth, was examined and testified as follows: [93]

The Clerk: Please state your name.

The Witness: J. Ervin Waters.

Direct Examination

By Mr. Tietz:

Q. Do you hold any particular position in the Church of Christ?

A. I am an evangelist of the Church of Christ.

Q. Are you an evangelist in the division of which this defendant is a member?

(Testimony of J. Ervin Waters.)

A. Yes, sir.

Q. Am I correct in referring to it as a "peace division"? A. Yes.

Q. What distinguishes it from the other divisions of the Church of Christ with respect to pacifism?

Mr. Real: Your Honor, I will object to the answer to this question as irrelevant to the issues in this case.

Mr. Tietz: I must concede that probably it was not too correct a question. L withdraw it.

Q. Do you know this defendant?

A. Yes, sir.

Q. How long have you known him?

A. Almost 14 years.

Q. How well have you had the opportunity to get acquainted with him and his associates?

A. During those 14 years sometimes [94] rather constantly and at others intermittently. I have been associated with him in church work and activities. I fact, a few years ago Montebello was my headquarters and the Los Angeles area was also for several years, and I have held a few meetings at the Church at Montebello, likewise at adjacent congregations or nearby congregations which the defendant has attended, and he has even visited in my home which presently is in Tennessee.

Q. Do you have means of knowing his reputation among his associates for truth and veracity?

A. Yes, sir.

Q. What is that reputation?

(Testimony of J. Ervin Waters.)

A. It is good.

Mr. Tietz: Thank you.

Mr. Real: No cross-examination, your Honor.

Mr. Tietz: We will call Floyd Morrow.

FLOYD W. MORROW, SR.

called as a witness by the defendant, having first affirmed to tell the truth, the whole truth and nothing but the truth, was examined and testified as follows:

The Clerk: State your name, please.

The Witness: Floyd W. Morrow, Sr.

Direct Examination

By Mr. Tietz:

Q. What is your occupation? [95]

A. I am an auto mechanic.

Q. Do you occupy any position in the Church of Christ?

A. I am a member of the Church of Christ.

Q. Do you know this defendant?

A. Yes, sir.

Q. How long have you known him?

A. Well, I knew him—I came here in '32, and if he was that old, I knew him that long, just how old he is. I knew him since 1932 or '33, since he was a child.

Q. Have you had the opportunity to get well acquainted with him? A. Oh, yes.

Q. How often have you seen him in the last few years? A. Often.

(Testimony of Floyd W. Morrow, Sr.)

Q. Well, when you say "often" do you mean, perhaps, once a week or what?

A. Well, sometimes oftener than that, sometimes maybe several weeks apart.

Q. Do you believe you have the means of knowing his reputation among his associates for truthfulness? A. I do.

Q. What is that reputation?

A. I don't know how it could be any better.

Mr. Tietz: Thank you. You may cross-examine.

Mr. Real: No cross-examination, your [96] Honor.

The Court: You may step down, Mr. Morrow.

Mr. Tietz: Our last witness, your Honor, will be Mr. Carl Hildebrand.

Mr. Real: In the interests of saving time, if this witness will testify to the truth and veracity of this defendant, we will stipulate that this witness will testify that his reputation for truth and veracity is good.

Mr. Tietz: We will accept that stipulation. Thank you very much, Mr. Hildebrand.

The defendant rests, your Honor. And we have a motion on another ground that will require a little argument.

The Court: Any rebuttal? Does the Government rest?

Mr. Real: The Government rests, your Honor.

The Court: Both sides rest. You wish to renew your motion for a judgment of acquittal?

Mr. Tietz: The defendant wishes to renew the motion that was made at the close of the Govern-

ment's case on the two separate points stated, and the defendant wishes to add to those two points a third point and would like to argue it. Possibly the court, after hearing the nature of the argument, might even want the matter briefed.

The nature of my argument is this: That this defendant was frustrated from securing a right given to every registrant, namely, an appeal; and that the intent of Congress that every registrant claiming to be a conscientious objector to any [97] form of participation in warfare should be determined. [98]

* * *

Mr. Real: Yes, your Honor. Does your Honor wish to rule on the motion now before the court for a judgment of [118] acquittal, your Honor?

The Court: Yes. The motion for a judgment of acquittal will be denied. [119]

The Court: The case is here for further trial. The evidence is still open, I take it?

Mr. Tietz: Yes, sir. We would have no objection whatever to the Government rebutting what the witness has testified to.

The Court: This defendant now rests?

Mr. Tietz: Yes, sir. We have no more testimony.

Mr. Real: No rebuttal testimony by the Government, your Honor.

The Court: Both sides rest?

Mr. Real: Both sides rest.

The Court: Any argument? [128]

* * *

Anything further?

Mr. Tietz: No, your Honor.

The Court: Very well, the defendant is found guilty as charged. [145]

* * *

The Court: Let the defendant come to the bar.

(Argument for mitigation of sentence omitted from transcript by request of counsel.)

The Court: Does the Government have anything?

Mr. Real: The Government's recommendation is for a penitentiary type of sentence, your Honor.

The Court: Do you have anything to say, Mr. Rowland?

Mr. Tietz: Might I have a word? Does the Government mean by "penitentiary type" a prison type sentence?

The Court: The Director of Prisons has the authority under the law to place any prisoner wherever he thinks he should be.

Mr. Tietz: But I do hope that when this young man is eligible for parole there won't be any feeling that his is an aggravated case, and I would like an expression that the United States Attorney feels that.

Mr. Real: There will be no feeling of that. Our recommendation of a penitentiary type sentence is a recommendation for sentence wherever the Attorney General feels that this man can best be used.

The Court: Anything further?

Mr. Tietz: Nothing, your Honor. [162]

The Court: Do you have anything you want to say, Mr. Rowland?

The Defendant: There is no need to waste words.

The Court: Pardon?

The Defendant: There is no need to waste words.

The Court: It might not be a waste of words. It is your opportunity to say what you want to say. You follow the dictates of your conscience and your conscience is clear, and you know the peace that goes with a person who works with a clear conscience.

The Defendant: I would like to ask what you think religious training and belief is. All of my life I have been taught about this, ever since I can remember, and I see no reason that you could say that I haven't been, and to say that you see anything in the file that says that I don't believe this.

The Court: I did not suggest that, Mr. Rowland.

The Defendant: That was my understanding of what you said.

The Court: If you got that impression, it is an erroneous impression. The file contains a clear statement of your belief and your local board apparently must have been convinced of the honesty and sincerity of your conscientious objection or you would not have been classified in 1-A-O. But, to have that classification, to my mind is a long way

from having a 1-O classification which is based upon religious [163] training and belief.

I do not know whether you follow the teachings of Christ or not. I assume you do.

The Defendant: I am a member of the Church of Christ.

The Court: And I did not know that Christ had ever taught and preached that a Christian would contaminate himself by coming into contact with unbelievers and sinners. In fact I always understood it contrary.

But that is not my province. That is for the local board and the appeal board of the Selective Service System. It may be General Hershey's duty at the top to do something about it. If he feels that the classification is wrong, it is the State Director's duty to do something about it, the appeal board, the local board, and your case has had the attention of the State Director and, I believe, the National Director.

Isn't that true, Mr. Tietz?

Mr. Tietz: They left it up to the court. They said the court is better able to judge.

The Court: You brought it to their attention?

Mr. Tietz: Oh, yes, yes.

The Court: It is not the court's function to classify. It is only the court's function to say whether or not there is any reasonable and rational basis for the classification given you by the draft board, and clearly there is. [164]

Anything further?

One of the great difficulties is that Congress does not go as far in granting exemptions as some people apparently do in claiming conscientious objections. But that has been true in all ages, hasn't it, in all history, that people with more sensitive consciences often suffer because the majority do not understand the extent of their conscientious convictions? And the Government, being accommodated not to either extreme, sometimes does not accommodate, or the law does not amply accommodate the extremely sensitive conscience, and it is those who have suffered throughout history.

Anything further? Do you have anything further, Mr. Rowland?

The Defendant: Nothing of any importance.

The Court: It is your time to say anything you wish to say.

The Defendant: I would like to say that I feel that the court is prejudiced against me and against any conscientious objector. It has been evident in this trial and I have seen other trials, and I feel that you are prejudiced.

That is all I have to say.

The Court: Mr. Rowland, I will treat you just the way I have treated all the others. I do not say this in reply to what you have just said. You are entitled to your opinion, of course. I merely say that for the comfort it might be [165] to you, that you can go back to 1946, when I first embarked upon having the unpleasant duty to sentence people such as you, and I think you will find that, even

though I am in error in your opinion, I have been consistently in error.

Anything further? Are you ready for sentence?

The Defendant: Yes.

The Court: It is the judgment of the court, Robert Donald Rowland, that you be committed to the custody of the Attorney General of the United States or his authorized representative for imprisonment for a period of four years for the offense charged in the indictment.

You are now committed to the custody of the Marshal to serve that sentence and your bail is exonerated.

[The omitted portions of The Reporter's Transcript consisted of argument of counsel.] [166]

CERTIFICATE

I hereby certify that I am a duly appointed, qualified and acting official court reporter of the United States District Court for the Southern District of California.

I further certify that the foregoing is a true and correct transcript of the proceedings had in the above-entitled cause on the date or dates specified therein, and that said transcript is a true and correct transcription of my stenographic notes.

Dated at Los Angeles, California, this 25th day of March, A.D. 1953.

/s/ ALBERT H. BARGION,
Official Reporter.

[Endorsed]: Filed April 7, 1953.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 16, inclusive, contain the original Indictment; Motion to Dismiss; Order Denying Motion to Dismiss; Waiver of Trial by Jury and of Special Findings of Fact; Motion in Arrest of Judgment; Motion for New Trail; Judgment and Commitment; Notice of Appeal and Designation of Record on Appeal and a full, true and correct copy of Minutes of the Court for October 27, 1952, February 9, 1953, and March 2, 1953, which, together with the original exhibits and Reporter's Transcript of Proceedings on October 27, 1952, transmitted herewith, constitute the record on appeal to the United States Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing and certifying the foregoing record amount to $2.80 which sum has been paid to me by appellant.

Witness my hand and the seal of said District Court this 9 day of April, A.D. 1953.

[Seal] EDMUND L. SMITH,
Clerk,

/s/ THEODORE HOCKE,
Chief Deputy.

[Endorsed]: No. 13800. United States Court of Appeals for the Ninth Circuit. Robert Donald Rowland, Appellant, vs. United States of America, Appellee. Transcript of Record. Appeal From the United States District Court for the Southern District of California, Central Division.

Filed April 10, 1953.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

United States Court of Appeals
for the Ninth Circuit

No. 13800

ROBERT DONALD ROWLAND,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON APPEAL

Appellant will rely upon the following points in the prosecution of his appeal from the judgment entered in the above-entitled cause.

I.

The District Court erred in not holding that the I-A-O classification was without a basis of fact

and that the failure to classify the registrant I-O was arbitrary.

II.

The District Court erred in not holding that the indictment was fatally defective.

III.

The District Court erred in not holding that the appellant had been frustrated in his desire to secure an administrative personal appearance and appeal.

/s/ J. B. TIETZ,
Attorney for Appellant.

[Endorsed]: Filed April 10, 1953.

[Title of Court of Appeals and Cause.]

ADOPTION OF DESIGNATION

Appellant hereby adopts the Designation of Record heretofore filed in the District Court.

/s/ J. B. TIETZ.

[Endorsed]: Filed April 10, 1953.

[Title of Court of Appeals and Cause.]

STIPULATION AMENDING ADOPTION OF DESIGNATION

It is hereby stipulated that the Adoption of Designation of Record, heretofore filed, may be amended to read that only the following portions of Reporter's Transcript are material to a proper consideration of the appeal:

* * *

The record is to show that omitted portions of the Reporter's Transcript consisted of argument of counsel.

Dated: April 24, 1953

/s/ J. B. TIETZ,
Attorney for Appellant.

WALTER S. BINNS,
United States Attorney,

By /s/ MANUEL L. REAL,
Asst. United States Attorney.

[Endorsed]: Filed April 27, 1953.

No. 13800

In the United States Court of Appeals

For the Ninth Circuit

ROBERT DONALD ROWLAND,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

Appellant's Opening Brief

J. B. TIETZ
257 S. Spring Street
Los Angeles 12, California
Attorney for Appellant.

TABLE OF CASES AND AUTHORITIES CITED

Cases

Codes and Authorities

In the
United States Court of Appeals
For the Ninth Circuit

ROBERT DONALD ROWLAND, *Appellant,* vs. UNITED STATES OF AMERICA, *Appellee.*	No. 13800

Appellant's Opening Brief

JURISDICTIONAL STATEMENT

This is an appeal from a judgment of conviction of the appellant by the District Court of the Southern District of California.

This court has jurisdiction under the provisions of 28 United States Code, Sections 1291 and 1294 (1).

STATEMENT OF THE CASE

Appellant was indicted on October 15, 1952 under U.S.C., Title 50, App. Sec. 462—Selective Service Act, 1948, for refusing to submit to induction [R. 3].[1]

[1]All references to the Transcript of Records are designated by pages of it, as follows: [R. 3]. A photocopy of the entire Selective Service File of appellant was entered in evidence as Government's Exhibit 2. The file is not part of the Transcript of Record but is before the court. All references to the file are designated as pages of Exhibit 2, as follows: [Ex. p. 3]; the pagination of Exhibit 2 is by a one-quarter inch high pencilled number, circled, and ordinarily is found at the bottom of each sheet of the Exhibit.

Appellant was convicted by Judge William C. Mathes on February 9, 1953; he was sentenced by said judge to a 4-year term of imprisonment on March 2, 1953. [R. 11-12.]

In the court below as well as before the Selective Service agencies, appellant claimed to be a conscientious objector to all participation in military activities and that he was entitled to a classification as such, to-wit: 1-O.

At his first opportunity, on November 6, 1950, he disclosed that he was a conscientious objector by signing Series XIV in the Classification Questionnaire. [Ex. p. 10.]

In his Special Form for Conscientious Objectors [Ex. pp. 12-15] he set forth the details requested concerning his religious training and his religious belief, including the following:

1. First, he chose to sign Series I—(B), thus indicating he was opposed to all participation in military service. [Ex. p. 12.]
2. He described his belief, answering series II—2 as follows:

> "I believe that it is wrong to kill, (Romans 13:9) that it is wrong to fight with carnal weapons (2 Corinthians 10:3-5; Ephesians 6:12; Matthew 26:52) and participate in carnal warfare (John 18-36). Since these are the duties of Military Services I can't join them, I also believe it is my duty to

meet with the Church of Christ on the first day of the week. I believe that I should obey the Lord rather than man." [Ex. p. 12.]

3. That the source of his training was:

"By studying the Bible for myself. From religious teaching in the Church of Christ, and from my Mother's training at home, both from my earliest remembrance." [Ex. p. 13.]

4. That his mother is a member of the Church of Christ and that he was baptised in it May 8, 1948. [Ex. p. 14.]*
5. He answered the question "5. Under what circumstances, if any, do you believe in the use of force?" "None—Luke 3:14." [Ex. p. 13.]
6. All his other answers, on pages 12 to 15 of Exhibit 2 were consistent and corroborative.

When the local board classified him in Class 1-A-O (Conscientious Objector Available for Noncombatant Military Service only) he promptly [R. 65, 66] went to the office of the local board to have a personal appearance and to appeal [R. 61, 62]. He considered his conversation there with the clerk his "personal appearance" [R. 61]; the clerk convinced him that he couldn't get the classification changed and, even more impor-

*This section of the Church of Christ is one of the historic pacifist groups. It has over 200 congregations and has a history, in America, of over 100 years as a pacifist organization: Attorney General File No. A. G. 000.31 and Congressional Record, May 7, 1942. [See Appendix C.]

tant, that there was nothing he could do [R. 62]; he also considered that his conversation with the clerk was the "appeal" mentioned in the Selective Service documents. [R. 68].

During the trial appellant complained that the Order to Report for Induction was invalid because the classification was without a basis of fact [R. 34-36] and that no valid basis or any basis existed for crediting the sincerity and genuineness of appellant's professions of religious conscientious objections on the one hand, by giving him a 1-A-O classification, and denying these professions on the other hand by refusing him the 1-O classification [R. 36-38]; second, that a failure in the proof existed, namely whether the classification had been made by a majority of the board and with a quorum present [R. 38-43]; and third, that he had been denied due process by being frustrated in his attempt to secure both a genuine personal appearance and the procedural appeal.

Appellant also had attacked the indictment as being insufficient. [R. 9.]

QUESTIONS PRESENTED

1. The board gave appellant a limited conscientious objector status. This 1-A-O classification made him liable for training and service in the armed forces for noncombatant military service.
   Was the 1-A-O classification arbitrary, capricious and without basis in fact?

2. The undisputed evidence showed that a variance existed between the numerical evidence of the voting on appellant's classification by the board and the written evidence.
   Was the trial court required to find, as a matter of law, that the written evidence governed, in determining whether or not the classification of appellant was made by less than a majority of the members present at the meeting and that the meeting itself was illegal for want of a quorum?

3. Was the indictment fatally defective?

4. Was the defendant frustrated in his attempt to secure a personal appearance and an appeal?

SPECIFICATION OF ERRORS

1. The District Court erred in not concluding that the 1-A-O classification and the denial of the full conscientious objector status were arbitrary, capricious and without basis in fact. [R. 58.]
2. The District Court erred in not holding that the motions [R. 58, 77] for judgment of acquittal should have been granted.
3. The District Court erred in not holding that the indictment was fatally defective. [R. 9, 83.]

ARGUMENT

I.

THE DENIAL OF THE TOTAL CONSCIENTIOUS OBJECTOR STATUS AND THE DECISION TO CLASSIFY IN CLASS 1-A-O (MAKING APPELLANT LIABLE FOR NONCOMBATANT MILITARY SERVICE) WERE ARBITRARY, CAPRICIOUS AND WITHOUT BASIS IN FACT.

Section 6 (j) of Title I of the Selective Service Act of 1948 (50 U.S.C. §456 (j)), provides, in part, as follows:

> "Religious training and belief in this connection means an individual's belief in a relation to a Supreme Being involving duties superior to those arising from any human relation, but does not in-

clude essentially political, sociological, or philosophical views or a personal code."

Section 1622.20 (a) of the Selective Service Regulations [32 C.F.R. 1622.20 (a)] provided[1]:

> "In Class 4-E shall be placed any registrant who, by reason of religious training and belief, is found to be conscientiously opposed to participation in war in any form and to be conscientiously opposed to participation in both combatant and noncombatant training and service in the armed forces."

Section 1622.6 of the Selective Service Regulations [32 C.F.R. 1622.6] provided[2]:

> "(a) In Class 1-A-O shall be placed every registrant who would have been classified in Class 1-A but for the fact that he has been found, by reason of religious training and belief, to be conscientiously opposed to combatant training and service in the armed forces."

The evidence submitted by the appellant establishes that he had sincere and deep-seated conscientious objections against combatant and noncombatant military service which were based on his "relation to a Supreme Being involving duties superior to those arising from any human relation." This material also showed that his belief was not based on "political, sociological, or

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[1]On 28 September 1951 the nomenclature changed: Class 4-E became Class 1-O.

[2]On 28 September 1951 the section number was changed to 1622.11; it is otherwise the same.

philosophical views or a merely personal code," but that it was based upon his religious training and belief as an observant member of the pacifist division of the Church of Christ.

There is not one iota of evidence that in any way disputes the appellant's proof submitted showing that he was a conscientious objector with scruples against all participation in military activity.

There is no question whatever on the veracity of the appellant. The question is not one of fact but is one of law. The law and the facts irrefutably establish that appellant is a conscientious objector opposed to combatant and noncombatant service.

In view of the fact that there is no contradictory evidence in the file disputing appellant's statements as to his conscientious objections and there is no question of veracity presented, the problem to be determined here by this Court is one of law rather than one of fact. The question to be determined is: Was the holding by the board (that the undisputed evidence did not prove appellant was a conscientious objector opposed to both combatant and noncombatant service) arbitrary, capricious and without basis in fact?

A decision directly in point supporting the proposition made in this case, that the 1-A-O classification (conscientious objector willing to perform noncombatant military service) is arbitrary and capricious is *United States v. Relyea,* No. 20543, United States Dis-

trict Court for the Northern District of Ohio, Eastern Division, decided May 18, 1952. In that case the district court sustained the motion for judgment of acquittal saying, among other things, as follows:

> "I think it would have been more difficult for the court to find the act of the Board was without any basis in fact if the Board had classified this man as 1-A rather than 1-A-O. They accepted the defendant's profession of sincere and conscientious objections on the religious grounds as being truthful, but they attempted, and in my opinion without any basis in fact, to assert that while he was sincere and conscientious, that sincerity and conscientiousness extended only to his active aggressive participation in military service and that he was not sincere in his statements that he was opposed to war in all its forms."

A similar holding was made by United States District Judge Murray in *United States v. Goddard,* No. 3616, District of Montana, Butte Division, June 26, 1952. The court, among other things, said:

> " . . . after due consideration, the Court finds that the evidence is insufficient to sustain a conviction for the reason that there is no basis in fact disclosed by the Selective Service file of defendant upon which Local Board No. 1 of Ravalli County, Montana, could have classified said defendant in Class 1-A-O, and therefore the said Board was without jurisdiction to make such classification of defendant and to order defendant to report for induction under such classification."

This case is distinguished from the facts in *Head v. United States,* 199 F. 2d 337 (10th Cir.), where the 1-A-O classification was held to be proper. In that case the Court of Appeals found a basis in fact in the selective service file on which it could be said Head's scruples extended only to killing. The basis was this: Head's answer to a question in the Special Form for Conscientious Objectors (SSS Form No. 150) showed that he relied on a certain minister for guidance in religious matters; the F.B.I. investigation revealed (as shown by the Hearing Officer's report) that the minister held the noncombatant service view. The Tenth Circuit apparently concluded Head was bound to hold the same views as his teacher. Also, facts were present in the *Head* case which tended to impeach the good faith conscientious objections of the registrant. Here the undisputed evidence showed that the appellant held the view that he could not take *any* part in military activity and there is no evidence whatsoever that any of his teachers or associates held the noncombatant view.

There is absolutely no evidence whatever in the draft board file that appellant was willing to do noncombatant military service. All of his papers and every document supplied by him staunchly presented the contention that he was conscientiously opposed to participation in both combatant and noncombatant military service. The board, without any justification whatever, held that he was a conscientious objector who was willing to perform noncombatant military service.

Never, at any time, did the appellant suggest or even imply that he was willing to do noncombatant military service. He, at all times, contended that he was unwilling to go into the armed forces and do anything as a part of the military machinery.

The board, without any grounds whatever, compromised appellant's claim for total conscientious objection and awarded him only partial conscientious objector status.

It was arbitrary for the board to grant only part of appellant's claim and his testimony and reject the balance. The board classified appellant as one who was willing to serve in the armed forces and perform noncombatant service. This finding flies directly in the teeth of the evidence. If the board gave appellant a 1-A classification it could be argued that the board had refused to believe him sincere. Obviously the board believed him sincere or it could not properly have given him the 1-A-O classification.

Congress did not tend to confer upon the draft boards arbitrary and capricious powers in the exercise of their discretion. They must follow the law when the facts are undisputed. If there is a dispute the boards have the jurisdiction to weigh the testimony. In the case of a denial of the conscientious objector status, if there is no dispute in the evidence and the documentary evidence otherwise establishes that the registrant is a conscientious objector, it is the duty of the court to hold that there is no basis in fact. It must conclude

that there is an abuse of discretion, and that the classification is arbitrary and capricious. It is submitted that such is the case here. The undisputed evidence shows that the appellant is a conscientious objector entitled to the 1-O classification. The denial of the classification is without basis in fact. The classification of 1-A-O flies in the teeth of the evidence. Such classification is a dishonest one, making it unlawful. *Johnson v. United States* (8th Cir.), 126 F. 2d 242, 247.

There is no basis in fact for the classification in this case because there are no facts that contradict the documentary proof submitted by the appellant. The facts established in his case show that he is a conscientious objector to noncombatant service and, therefore, the classification given is beyond the jurisdiction of the boards.

It is respectfully submitted that the motion for judgment of acquittal should have been sustained because there is no basis in fact for the classification given by the draft boards and the denial of the total conscientious objector classification was arbitrary and capricious.

Counsel believes the decision of this court can and should be a definitive statement on the problem involved; that the Selective Service System and the District Courts will welcome such a definitive statement.

The attention of the court is invited to Appendices A and B wherein are found further comments on this

problem by two informed and thoughtful conscientious objectors.

II.

THE INDICTMENT IS FATALLY DEFECTIVE

The indictment [R. 3] is fatally defective because inextricably contained in it are incorrect references to the former Act.

The Selective Service Act of 1948 was amended on June 19, 1951, by being completely replaced by the Universal Military Training and Service Act.

Appellant's refusal to submit to induction, the basis for this prosecution and conviction, occurred on July 28, 1952.

The caption of the indictment spells out the obsolete Act; the body of the indictment is reproduced below, certain portions being underlined to emphasize the essentiality of the offensive references to the obsolete Act:

> "The grand jury charges:
>
> "Defendant ROBERT DONALD ROWLAND, a male person within the class made subject to selective service *under the Selective Service Act of 1948,* registered as required *by said act and the regulations promulgated thereunder* and thereafter became a registrant of Local Board No. 113, said board being then and there duly created and acting, under the Selective Service System *estab-*

lished by said act, in Los Angeles County, California, in the Central Division of the Southern District of California; *pursuant to said act and the regulations promulgated thereunder,* the defendant was classified in Class 1-A-O and was notified of said classification and a notice and order by said board was duly given to him to report for induction into the armed forces of the United States of America on July 28, 1952, in Los Angeles County, California, in the division and district aforesaid; and at said time and place the defendant did knowingly fail and neglect to perform a duty required of him *under said act and the regulations promulgated thereunder* in that he then and there knowingly failed and refused to be inducted into the armed forces of the United States as so notified and ordered to do."

Since the indictment is a pleading its sufficiency must be determined by the facts therein set forth.

Taylor v. United States, 2 F. 2d 444, 446.

Where reference to a statute in an indictment is essential for the reason that the indictment would otherwise be lacking in necessary allegations an incorrect reference to the statute may be fatal.

"The ancient rules as to the effect of even a slight error in the recital of a statute in an indictment have been much relaxed. Where the reference to the statute must be considered because the indictment is senseless, or lacking in essential alle-

gations unless the reference is considered, a misrecital may be fatal; but, if an offense is otherwise fully stated in an indictment, a mistaken reference to a statute is surplusage and does not render the indictment invalid."

Johnson v. Biddle, 12 F. 2d 366.

"The offense laid in an indictment is charged by the allegations of fact not by reference to statutes. If reference to a statute is essential for the reason that the indictment does not make sense or is lacking in necessary allegations without it, an incorrect reference may be fatal."

Martin v. United States, 99 F. 2d 236.

Public Law 51, 82nd Congress (Universal Military Training and Service Act) approved June 19, 1951, Title I, Section 1, amended section 1 (a) of the Selective Service Act of 1948 (62 Stat. 604) as amended so as to provide that said act was to be cited as the "Universal Military Training and Service Act."

The indictment in the case at bar and each allegation of fact in such indictment is based and is dependent on the "Selective Service Act of 1948" when, in fact, there was no such act, as such in full force and effect at the time of the alleged offense.

A common law crime is not involved in the case at bar. It is submitted that to allege the crime the indictment appears to attempt to allege, reference to the ap-

plicable statute is essential for the reason the indictment would otherwise be lacking the necessary allegations of fact. While reference to a statute is made in allegations of fact in the indictment in the case at bar the reference made is erroneous. For that reason the indictment does not allege any crime whatsoever.

It is true that where an offense is sufficiently charged an incorrect reference to a statute does not render the indictment invalid. That rule is inapplicable where a reference to a statute and the regulations promulgated thereunder are necessary in order to sufficiently charge the crime upon which the indictment is based.

For the reasons expressed above the indictment of Robert Donald Rowland in this case should have been dismissed.

III.

THE CLASSIFICATION OF APPELLANT WAS MADE AT AN ILLEGAL MEETING OF THE BOARD.

The factual basis for this point and the argument, with its supporting references, are fully set forth in the Transcript of Record, pp. 38-43.

The citation for the case of *Ohl vs. Smith* referred to therein, is 288 U. S. 170, 177.

IV.

THE DEFENDANT WAS FRUSTRATED IN HIS ATTEMPT TO APPEAL AND WAS THEREBY DENIED DUE PROCESS.

Every dissatisfied Selective Service registrant is offered an opportunity to have the State Appeal Board pass on the merits of his claims for a deferred or exempt classification [§1626.2].

Every Selective Service registrant, professing to be a conscientious objector, but denied a 1-O classification by the local board is offered an opportunity to have the merits of his claims evaluated and determined by the State Appeal Board after certain "special provisions" relating to such registrants are followed. These special provisions include an intensive investigation by the Federal Bureau of Investigation, an un-

hurried hearing by a Hearing Officer of the Department of Justice, a lengthy analysis by him to the Attorney General and an analysis and recommendation by the Attorney General to the State Appeal Board.

Every dissatisfied Selective Service registrant is also offered an opportunity to make a personal complaint to the local board. At all other times he may contact only the clerk. The clerk is the only salaried employee. Her patience is tested every day. She has a great load of paper work and must also be the buffer between the registrant, his mother and the board. Sometimes she protects the board too well; the concise and to the point evidence in this case reveals that this occurred [R. 62].

Appellant had no genuine appeal; nor did he have a true personal appearance. Promptly after receiving the Classification Notice he attempted to appeal. He did this by going to the government official who mailed him the notice and discussed with her his dissatisfaction with the classification. When she told him the board wouldn't change the classification he asked her if there was anything he could do and she told him there wasn't [R. 62]. There was no rebuttal to this evidence.

All the clerk had to do was to say to him "Write on this piece of paper the words 'I appeal' and then sign your name." In any event she was under a duty not to mislead him by telling him that nothing could be

done. In *Rock Island, A. and L. R.R. v. United States,* 254 U. S. 141, at 143 Mr. Justice Holmes declared "Men must turn square corners when they deal with the Government." Appellant believes it follows that a 19 year old citizen can expect the same standard of right-angled rectitude from his government's officials.

Appellant submits that the record demonstrates that this local board official frustrated him in perfecting his appeal and that it demonstrates that he never intended to waive his right to an appeal. Counsel asserts to the court that he has learned that two clerks in the Los Angeles area have been discharged for so frustrating registrants and that all clerks of this area have been instructed to place a sheet of paper in front of each registrant who presents himself at the local board office, within the 10-day appeal period, complaining of his classification, and to tell him to write on the paper the two words "I appeal" and then sign his name.

Selective Service registrants at the present time are all young and inexperienced; they should not be held to the same appeal formalities, the same degree of skepticism towards statements by minor governmental functionaries and the same judgment that is expected of lawyers or even of lay adults.

> *Cox v. Wedemeyer,* 192 F. 2d 920, 922-923 (9 C. A.).

In his last reported decision before becoming Attorney-General Judge McGranery held, in *Ex Parte Fabiani,* 105 F. Supp. 139:

> "The different objective to be achieved by the new Act behooves us to employ a more liberal standard of judicial review, so as better to protect the rights of the individual. Should—which God forbid—world tension increase greatly or should general war come, then the judicial arm can once again cut to the barest minimum its supervision of the operations of the draft." [146-147.]

A number of courts have concluded that Selective Service registrants were frustrated, under very similar circumstances:

United States ex rel. Filomio v. Powell, 38 F. Supp. 183

> Regulations then in force provided the registrant was to appeal on a form to be attached to his classification questionnaire.
>
> On p. 187 the Court observed: "Evidence is conflicting as to whether Filomio demanded the questionnaire in order that he might perfect his appeal. We do not feel that it was readily available, and hence his omission in this respect was beyond his control." [187]

United States ex rel. Beye v. Downer, 143 F. 2d 125

> Registrant was deprived of a right to appeal by the local board deliberately frustrating him.

Facts: Board persuaded Army to waive medical certificate of acceptability [after registrant had been found to be eligible for a 4-F classification] by writing Army "This man has been a complete nuisance."

C.C.A. 2 reversed a decision that had denied petitioner a writ.

Ex Parte Hutflis, 245 F. 798 (W.D.N.Y. 1917)

This W.W.I. petitioner asserted

1. Through ignorance his claim to exemption [alien] was not filed:
2. That he was misled by a member of the board, though unintentionally, as to the method of filing his claim for exemption.

(He applied to the local board for a form upon which to file his claim for exemption, and was given by mistake an appeal blank)

Q. Did relator waive his privilege of asserting an exemption?

On page 800 the Court held: "It seems to me, under the circumstances, that waiver is of doubtful application for at no time did the relator intend to relinquish any rights . . . relator has had no hearing whatsoever, his evidence is not in, and his right to exemption has not been passed upon."

SUMMARY

The appellant's selective service file reveals that there was no basis in fact for classifying appellant in a 1-A-O classification and that there was no factual basis for making a distinction between his claims and his deserts.

The trial evidence does not contain sufficient proof that appellant had been classified at a meeting of the board where a quorum was present or that he had been classified by a majority of those present or that all present had voted.

The indictment reveals that it was fatally defective.

The unrebutted trial evidence shows that appellant had been frustrated in his attempt to secure a true appearance before the local board and a true appeal.

Respectfully submitted,

J. B. TIETZ,
Attorney for Appellant.

Appendix

APPENDIX "A"

With reference to the correspondence that you and A. J. have had about suggestions for draft boards which would facilitate deciding which men were entitled to 1-O and which to 1-A-O classifications. I think that the only additional comment that I have to offer is an expression of hope that, whenever a young man asks for a 1-O classification, he not be given the 1-A-O classification unless the evidence clearly indicates that he should be put in 1-A-O. The main reason for saying this is that in this area, particularly in the hearings of a now-deceased hearing officer, there used to be some questions asked that came almost in the category of trick questions. The principal one of these was a question as to whether the registrant would have any objection to doing hospital work on behalf of injured soldiers. If the registrant said yes, then there was almost no chance that he could get a recommendation for a 1-O position. This and similar questions never seemed to be asked in such a context as to bring out anything like the total import of doing non-combatant work. The question suggested that non-combatant work consisted almost exclusively of work in hospitals, which I believe is not true. Where we have had opportunities to advise registrants ahead of time as to what questions might be asked them, we warned them about this particular question and about its total import.

Whatever the situation now in this and other areas, if something can be done to induce Selective Service officials to base 1-A-O classifications in situations where 1-O is sought on more substantial evidence than a simple yes to a question of this sort, that would seem to me to help prevent some of these controversies from arising about the 1-A-O classification and to be of general service to COs.

APPENDIX "B"

In re your query about the suggestion made by Judge Mathes that "some type of instructions for draft boards that would help them determine the difference between the 1-A-O and the 1-O position" should be prepared.

The law requires that the Selective Service Board and the appeal machinery decide if an applicant is conscientiously opposed on grounds of religious training and belief to combatant participation in the armed forces (1-A-O) or opposed to noncombatant as well as combatant service in the armed forces (1-O). This imposes upon the board, etc. the difficult—some would say impossible—task of determining whether the applicant is "sincere" and whether in taking either the 1-O or the 1-A-O position he does so on grounds of religious training and belief. It seems to me to follow that once a board decides that a man is "sincere" and "religious"—and this is clearly implied if it is prepared to put the applicant either in 1-O or 1-A-O, a board would have no more right to put a man in the latter than in the former classification if it has doubts about his being "sincere" or "religious"—than the decisive, and perhaps the only, criterion whether the man should go in 1-O or 1-A-O is the man's own say-so.

If the board decides that an applicant who asks for 1-O is not entitled to that classification, it would appear

that it must do so either because it believes the applicant is mistaken in asking for 1-O instead of 1-A-O or that he is dishonest. (For example, he wants to be kept out of range of gun fire.) If the former is the case, and the man is honestly mistaken as to the classification in which he belongs, he can readily be convinced of this by persuasion. If, as I sense is usually thought to be the case, the board believes that the applicant is dishonestly seeking 1-O when he actually belongs in 1-A-O, it has no right, as I see it, to give him either 1-O or 1-A-O. It has to regard him as a draft evader in the invidious sense of the term.

Presumably, a draft board feels it to be its duty to get all able-bodied men of draft age into the armed forces. But Congress has imposed a limitation of this responsibility of draft officials to man the armed forces, namely that they may not coerce the conscience of one sincerely opposed to all war on the grounds of religious training and belief. The obligation to get every able-bodied man into the armed forces is in such case superceded by the obligation not to coerce conscience. Again, therefore, if an applicant is adjudged "sincere" and "religious" and said applicant states that he is unalterably and conscientiously opposed to noncombatant as well as combatant service in the armed forces, the board would seem to have no more right to force him into 1-A-O than it has a right to force a sincere and religious youth who asks for 1-A-O into armed service (1-A).

A couple of observations on what supposedly makes the individual decide that he belongs in 1-O or 1-A-O, may be relevant.

1. The C.O. is always confronted with the fact that in a highly integrated society and in a period when war tends to be total, the individual cannot extricate himself in an absolute sense from that society or from some implication to war. The food which the farmer raises may be used to feed soldiers and munitions workers. Even the so-called absolutist C.O. who will not even register and who submits to imprisonment rather than violate his conscience, is faced in prison with the question as to whether cooperativeness there indirectly helps the war effort, whether he is putting his integrity in question by accepting food and housing from a war making government, etc. In such situation one sincere person will feel that where there is no such thing as a perfectly logical point at which to draw the line he has to draw it at performing combatant service. Another equally sincere person may be inwardly assured that he has to draw it against any service in the armed forces. One will feel that his responsibility to society and God requires him to "go along" with the government as far as he can; another equally sincere person may feel that his responsibility requires him to make as complete a break with war and with the war establishment as he possibly can.

Incidentally, the stage in his development as an individual and particularly as a C.O. may well have some-

thing to do with the stand an individual takes. It is important to weigh this factor at a time when young men have to make the decision about draft status at a very early age. Admittedly, there are cases when men have found themselves in the armed services before they realized what military action meant and before they themselves had attained conscientious scruples. Also, there are admittedly cases when men found themselves enrolled in the armed forces before they knew that the law made any provision for conscientious objection. In these circumstances, it is entirely possible that a man in first filling out his questionnaire may ask for 1-A-O, and, on the basis of my previous analysis, be fully entitled to the 1-O classification.

2. The 1-A-O position is the "easier" one to take, since the individual does not in that case stand apart from his fellows but is enrolled in the armed forces as they are. Few young men at 18 or 19 are likely to want to face, or be emotionally mature enough to be able to face, social disapproval resulting from failure to be inducted. As already suggested, it is exceedingly difficult to analyze and determine motives. No Selective Service Board is equipped with the professional help, for example, that would be needed to do anything like a scientific job; but in so far as motivation may be assessed by laymen it may, I think, be said that if anything, there is more reason to question the "sincerity" of one asking for a 1-A-O than of a person who is willing to face the strong social disapproval entailed

by refusal to render even noncombatant service. In so far as this line of thought is valid at all, it provides another reason why, once a board has determined that a person is a conscientious objector, it should give him the classification for which he asks.

3. There are some sects, notably the Seventh Day Adventists, who hold taking the 1-A-O position as virtually a condition of membership. This is both in the sense that a member of draft age may not engage in combatant service and in the sense that he may not refuse to render noncombatant service. Presumably where Congress has laid so much emphasis on "religious training and belief" considerable weight should be given to this fact.

4. Other sects, notably Jehovah's witnesses, make it virtually a condition of membership that one may not be enrolled in the armed forces at all. In general, it seems to me the law with its strong emphasis on "religious training and belief" requires that Selective Service officials attach great weight to such teachings.

APPENDIX "C"

Congressional record proceedings and debates of the 82nd Congress, Second Session of the Church of Christ on participation in Carnal welfare extension of remarks of Hon. Chet Holifield of California in the House of Representatives, Wednesday, May 7, 1952:

MR. HOLIFIELD: Mr. Speaker, under unanimous consent, I include a statement prepared by the Churches of Christ which I am placing in the Record at the request of Rev. C. Nelson Nichols, of Hollywood, Calif., one of the ministers signing the statement.

This statement sets forth the principles subscribed to by members of the Churches of Christ in regard to participation in carnal warfare.

1. The following is the substance of an open letter subscribed to by these Churches of Christ—recognized by the FBI as the "peace" Church of Christ:

"To whom it may concern:

"This is to certify that we Churches of Christ are conscientiously opposed to participation in war in any form. Our belief in the Supreme Being involves duties superior to those arising from any human relation. The basis of this faith is found in a multitude of Holy Scriptures, some of which follow: Matthew 26:48-52; Acts 5:29; Romans 12:19-21; Second Corinthians 10:3-5; Ephesians

6:10-17; Exodus 20:13; Matthew 5:21; Romans 13:9.

Our position on this vital subject has been set forth many times in this country by our ministers across the Nation. Alexander Campbell set forth these principles in his Address on War, in 1848, at Wheeling, W. Va., and it was published again in 1866 in Popular Lectures and Addresses of Alexander Campbell. On file in Washington, D. C., under file No. A. G. 000.31, are letters signed by many of our brethren stating our position on this subject. The book, Old Paths Pulpit, published by Homer L. King, Route 2, Lebanon, Mo., contained a recent work on this subject. The Old Paths Pulpit is a book of 33 written sermons by as many preachers and evangelists, and one, The Christian and Carnal Warfare, written by Paul O. Nichols, 849 Wilcox Avenue, Hollywood, Calif., sets forth our position in more recent times. This sermon represents a recent pronouncement, publicly made, of our religious position with regard to participation in carnal warfare.

"We do not know of an active minister in these Churches of Christ who does not oppose Christians participating in carnal warfare. These Churches of Christ are not to be confused with many which wear the same name; we constitute a distinct fellowship.

"We submit this that all may know our position relative to our opposing participation in carnal warfare, and that we might be recognized as a distinct group or fellowship which now is and in

the past has been 'a peace church,' to use modern terminology."

2. Excerpt from A. Campbell's Address on War in 1848 (p. 10):

> "We should inspire a pacific spirit, and urge on all proper occasions the chief objections to war. We must create a public opinion on this subject. . . . War creates and perpetuates national jealousy, fear, hatred, and envy. It arrogates to itself the prerogative of the Creator alone, to involve the innocent multitude in the punishment of the guilty few. It corrupts the moral taste and hardens the heart; cherishes and strengthens the base and violent passions; destroys the distinguishing features of Christian charity—its universality and its love of enemies; turns into mockery and contempt the best virtue of Christians—humility; weakens the sense of moral obligations; banishes the spirit of improvement, usefulness, and benevolence; and inculcates the horrible maxim that murder and robbery are matters of state expediency."

3. Excerpt from Paul O. Nichols' Christian and Carnal Warfare, published in 1945:

> "We, as Christians, are as out of place engaging in a carnal conflict, as the world would be trying to fight the spiritual warfare. The world cannot fight the spiritual fight, without first becoming spiritual; no more can a Christian fight a carnal conflict without first becoming carnal."

4. In regard to selective-service registrants:

> "This body or fellowship has and is gaining recognition as to its unity regarding nonparticipation in carnal warfare. Each young man studies for himself the various aspects of the question, forms his own belief, and takes his own stand on his convictions. The church influences his position only in teaching and offering scriptural references for his personal study and then stands behind him wholeheartedly in encouragement and moral support"—C. Nelson Nichols.

Reference may be made to or information obtained from the following men who are closely associated with the work of these Churches of Christ: Homer L. King, route 2, Lebanon, Mo.; Homer A. Gay, Lebanon, Mo.; D. B. McCord, Glendora, Calif.; J. Ervin, Waters Lawrenceburg, Tenn.; C. Nelson Nichols, 849 Wilcox Avenue, Hollywood, Calif.

No. 13800.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ROBERT DONALD ROWLAND,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

REPLY BRIEF OF APPELLEE.

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No. 13800.

IN THE

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FOR THE NINTH CIRCUIT

ROBERT DONALD ROWLAND,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

REPLY BRIEF OF APPELLEE.

I.
STATEMENT OF JURISDICTION.

Appellant was indicted by the Federal Grand Jury in and for the Southern District of California, on October 15, 1952, under Section 462 of Title 50, App., United States Code, for refusing to submit to induction into the armed forces of the United States. [R.[1] pp. 3-4.]

On October 27, 1952, the appellant was arraigned, entered a plea of Not Guilty, and the case was set for trial on November 24, 1952. [R. p. 4.]

On December 23, 1952, trial was begun in the United States District Court for the Southern District of California, by the Honorable William C. Mathes, without a jury, and on February 9, 1953, the appellant was found guilty as charged in the Indictment. [R. p. 78.]

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[1]"R." refers to Transcript of Record.

On March 2, 1953, appellant was sentenced to imprisonment for a period of four years and judgment was so entered. [R. p. 82.] Appellant appeals from this judgment.

The District Court had jurisdiction of this cause of action under Section 462 of Title 50, App., United States Code, and Section 3231 of Title 18, United States Code.

This Court has jurisdiction under Section 1291 of Title 28, United States Code.

II.
STATUTES INVOLVED.

The Indictment in this case was brought under Section 462 of Title 50, App., United States Code.

The Indictment charges a violation of Section 462 of Title 50, App., United States Code, which provides, in pertinent part:

> "(a) Any . . . person charged as herein provided with the duty of carrying out any of the provisions of this title [sections 451-470 of this Appendix], or the rules or regulations made or directions given thereunder, who shall knowingly fail or neglect to perform such duty . . . or who in any manner shall knowingly fail or neglect to perform such duty . . . or who in any manner shall knowingly fail or neglect or refuse to perform any duty required of him under oath in the execution of this title [said sections], or rules, regulations, or directions made pursuant to this title [said section] . . . shall,

upon conviction in any district court of the United States of competent jurisdiction, be punished by imprisonment for not more than five years or a fine of not more than $10,000, or by both such fine and imprisonment . . ."

III.
STATEMENT OF THE CASE.

The Indictment returned October 15, 1952, charges that the defendant was duly registered with Local Draft Board No. 113, was thereafter classified I-A-O, notified to report for induction into the armed forces on July 28, 1952, and that defendant thereafter knowingly failed and refused to be inducted into the armed forces.

On October 27, 1952, appellant appeared for arraignment and plea, represented by E. H. Hiber, Esq., before the Honorable William C. Mathes, United States District Judge, and entered a plea of Not Guilty to the offense charged in the Indictment.

On December 23, 1952, the case was called for trial before the Honorable William C. Mathes, United States District Judge, without a jury, and on February 9, 1953, the appellant was found guilty as charged in the Indictment. [R. p. 78.]

On March 2, 1953, appellant was sentenced to imprisonment for a period of four years. [R. pp. 11-13.]

Appellant assigns as error the judgment of conviction on the following grounds:

A—The District Court erred in not concluding that the I-A-O classification and the denial of the full conscientious objector status were arbitrary, capricious and without basis in fact. (App. Spec. of Error 1—App. Br. p. 6.)[2]

B—The District Court erred in not holding that the motion for judgment of acquittal should have been granted. (App. Spec. of Error 2—App. Br. p. 6.)

C—The District Court erred in not holding that the indictment was fatally defective. (App. Spec. of Error 3—App. Br. p. 6.)

IV.
STATEMENT OF THE FACTS.

On November 4, 1949, Robert Donald Rowland registered under the Selective Service System with Local Board No. 113, Pasadena, California. He was eighteen years of age at the time, having been born on October 26, 1931. He gave his occupation as "Student."

On November 1, 1950, Robert Donald Rowland filed with Local Board No. 113, SSS Form 100, Classification Questionnaire, and by signing Series XVI of that questionnaire, notified the Local Board that he claimed exemption from military service by reason of his conscientious objection to participation in war. He also requested further information and forms.

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[2]"App. Spec. of Error" refers to "Appellant's Specification of Errors"; "App. Br." refers to "Appellant's Brief."

SSS Form 150, Special Form for Conscientious Objector was furnished Rowland and he completed this form and filed it with Local Board No. 113 on November 6, 1950. Rowland claimed to be conscientiously opposed to participation in war in any form and also to participation in noncombatant training or service in the armed forces. This claim was made by reason of religious training and belief.

On November 15, 1950, Robert Donald Rowland was classified I-A-O by Local Board No. 113.

On November 21, 1950, Rowland was mailed SSS Form 110, Notice of Classification, notfiying him of the action of the Local Board.

On March 8, 1951, Rowland was mailed SSS Form 223, Order to Report for Armed Forces Physical Examination.

On April 2, 1951, Rowland was found to be acceptable for induction into the armed forces.

On July 16, 1952, SSS Form 252, Order to Report for Induction, was mailed to Rowland, ordering him to report for induction into the armed forces of the United States on July 28, 1952, at Los Angeles, California.

On July 28, 1952, Rowland reported for induction as ordered, but refused to submit to induction into the armed forces of the United States.

V.
ARGUMENT.

A. The Classification of the Appellant by the Local Board in Class I-A-O Was a Valid Classification.

The classification of registrants by Local Boards is provided by 50 U. S. C. A., App., Section 460, which provides in pertinent part:

> ". . .
>
> (b) The President is authorized—
>
> (3) To create and establish . . . local boards . . . Such local boards, . . . shall, under rules and regulations prescribed by the President, have the power . . . to hear and determine, . . . all questions or claims, with respect to inclusion or exemption or deferment from, training and service under this title (said sections), of all individuals within the jurisdiction of such local boards. The decisions of such local boards shall be final, except where an appeal is authorized and is taken in accordance with such rule and regulations as the President may prescribe . . ."

The limitations placed upon a trial court in the review of the classification given a Selective Service registrant were defined in the case of *Cox v. United States,* 332 U. S. 442. The Court in the *Cox* case, *supra,* says at page 448:

> "The scope of review to which petitioners are entitled, however, is limited; as we said in Estep v. United States, 327 U. S. 114, 122-3: 'The provision making the decisions of the local boards "final" means to us that Congress chose not to give administrative action under this Act the customary scope of judicial review which obtains under other statutes. It means

that the *courts are not to weigh the evidence* to determine whether the classification made by the local boards was justified. *The decisions of the local boards made in conformity with the regulations are final even though they may be erroneous.* The question of jurisdiction of the local board is reached only if there is no basis in fact for the classification which it gave the registrant.' " (Emphasis added.)

Appellant contends that there is no contradictory evidence in the file disputing appellant's statements as to his conscientious objections or veracity, and that therefore, the action of the Board in classifying him in Class I-A-O was arbitrary, capricious and without basis in fact. A reading of the appellant's Selective Service file [Government's Exhibit 2], would indicate the contrary.

Selective Service Regulations, Section 1622.6 (32 C. F. R. 1622.6) provided:

"1622.6 Class I-A-O: Conscientious Objector Available for Noncombatant Military Service Only.—

(a) In Class I-A-O shall be placed every registrant who would have been classified in Class I-A but for the fact that he has been found, by reason of religious training and belief, to be conscientiously opposed to combatant training and service in the armed forces.

(b) Section 6(j) of Title I of the Selective Service Act of 1948, provides in part as follows: 'Religious training and belief in this connection means an individual's belief in a relation to a Supreme Being involving duties superior to those arising from any human relation, but does not include essentially political, sociological, or philosophical views or a merely personal moral code.' "

Selective Service Regulations, Section 1622.20 (32 C. F. R. 1622.20) provided:

> "1622.20 Class IV-E: Conscientious Objector Available for Civilian Work Contributing to the Maintenance of the National Health, Safety or Interest—
>
> (a) In Class IV-E shall be placed every registrant who would have been classified in Class 1-A but for the fact that he has been found, by reason of religious training and belief, to be conscientiously opposed to participation in war in any form and to be conscientiously opposed to participation in both combatant and noncombatant training and service in the armed forces.
>
> (b) Section 6(j) of Title I of the Selective Service Act of 1948 provides in part as follows: 'Religious training and belief in this connection means an individual's belief in a relation to a Supreme Being involving duties superior to those arising from any human relation, but does not include essentially political, sociological, or philosophical views or a merely personal moral code.' "

These sections of the Selective Service Regulations define in broad terms the qualifications necessary for classification as a conscientious objector in classifications I-A-O and IV-E. The application of these descriptions to particular registrants is a duty imposed upon the Local Boards. The Local Board was left to determine how and when a registrant claiming exemption from military service by reason of conscientious objection was to be qualified. The exercise of that discretion, even though it may

have been erroneous, is final, in the absence of arbitrary or capricious conduct on the part of the Local Board so classifying a registrant.

Cox v. United States, supra.

To aid the Local Board in its determination of the conscientious objector claims of registrants, the Selective Service System uses SSS Form 150, Special Form for Conscientious Objector. The questions and answers given thereto by a registrant are the basis of a classification by a Local Board within the broad terms of Selective Service Regulations, Sections 1622.6 and 1622.20. The burden is upon the registrant to maintain and prove his claim within these categories. *Davis v. United States,* 203 F. 2d 853. This burden was not met by the appellant in the present case as evidenced by the classification given him by the Local Board.

Assuming the classification given this appellant were erroneous, this Court in the case of *Dickinson v. United States,* 203 F. 2d 336, said at page 345:

> "Even if we were of the opinion that the finding of the local board was clearly erroneous, and that it should have classified appellant as a minister of religion, we cannot on that basis alone hold the action of the draft board to be illegal, and the same limitations apply to the district court . . . Surely a part of the local board's duty, and a *part of its jurisdiction, involved using its common sense in deciding whether such a claim as this was worthy of belief.*" (Emphasis added.)

A reading of the record in the instant case presents no circumstances which discloses any bias, prejudice or unreasonable conduct on the part of the Local Board in the classification of the appellant. The trial court, therefore, properly denied appellant's motion for judgment of acquittal.

B. Appellant Was Convicted Under an Indictment Properly Reciting an Offense Against the United States.

The certainty required in an indictment is only such as will fairly inform the defendant of the crime intended to be alleged, so as to enable him to prepare for his defense and so as to preclude a second prosecution for the same offense.

Boyce Motor Lines v. United States, 342 U. S. 846;

Ross v. United States, 180 F. 2d 160.

Error in the citation of a statute is not fatal so long as an offense against the United States is charged.

Williams v. United States, 168 U. S. 382;

United States v. Hutcheson, 312 U. S. 219.

The test of the sufficiency of an indictment is whether the indictment contains the elements of the offense intended to be charged and sufficiently apprises the defendant of what he must be prepared to meet.

Hagner v. United States, 285 U. S. 427.

A one-count indictment was returned against the appellant by the Federal Grand Jury on October 15, 1952. It provides:

"In the United States District Court, in and for the Southern District of California, Central Division.

September, 1952, Grand Jury.

United States of America, Plaintiff, v. Robert Donald Rowland, Defendant. No. 22530-CD.

INDICTMENT.

[U. S. C., Title 50, App., Sec. 462—
Selective Service Act, 1948]

The grand jury charges:

Defendant ROBERT DONALD ROWLAND, a male person within the class made subject to selective service under the Selective Service Act of 1948, registered as required by said act and the regulations promulgated thereunder and thereafter became a registrant of Local Board No. 113, said board being then and there duly created and acting, under the Selective Service System established by said Act, in Los Angeles County, California, in the Central Division of the Southern District of California; pursuant to said act and the regulations promulgated thereunder, the defendant was classified in Class I-A-O and was notified of said classification and a notice and order by said board was duly given to him to report for induction into the armed forces of the United States of America on July 28, 1952, in Los Angeles County, California, in the division and district aforesaid; and at said time and place the defendant did knowingly fail and neglect to perform a duty required of him under said act and the regulations promulgated there-

under in that he then and there knowingly failed and refused to be inducted into the armed forces of the United States as so notified and ordered to do.

A True Bill.

Walter S. Binns,
United States Attorney.

ADM:AH

.....
Foreman."

Appellant contends that this indictment as returned by the Grand Jury fails to charge an offense against the United States. He contends that he was indicted for violation of the Selective Service Act of 1948 whereas the offense, if any, was a violation of the Universal Military Training and Service Act.

The Selective Service Act of 1948 was enacted on June 24, 1948, to provide an adequate armed strength to insure the security of the United States.

In order to provide for the increasing needs of the military establishment, the Congress enacted on June 19, 1951, the Universal Military Training and Service Act, amending the Selective Service Act of 1948. Among its provisions the 1951 amendments, Section 1(a), changed the title of the Act from "Selective Service Act of 1948" to "Universal Military Training and Service Act." Basically, however, the text of the Selective Service Act of 1948 was left unchanged.

The defect claimed to exist in the Indictment in the present case is that it "is based and is dependent on the 'Selective Service Act of 1948.'" A reading of the Indictment in its most essential parts and without reference

to any statute would indicate otherwise. The Indictment would then provide in its pertinent part:

> ". . . the defendant was classified in Class I-A-O and was notified of said classification and a notice and order by said board was duly given to him to report for induction into the armed forces of the United States of America on July 28, 1952 . . .; and at said time and place the defendant did knowingly fail and neglect to perform a duty required of him . . . in that he then and there knowingly failed and refused to be inducted into the armed forces of the United States as so notified and ordered to do."

The quoted portion of the Indictment provides all of the elements required to establish an offense against the United States, as provided in Title 50, App., United States Code, Section 462. These elements are shown to exist without reference to any statute in the Indictment. It is submitted that the appellant was fairly informed of the crime intended to be alleged in the Indictment; that the Indictment was sufficiently clear so as to enable the appellant to prepare his defense; and that it precluded a second prosecution for the same offense, within the meaning of the *Boyce* case, *supra.*

The appellant further contends that reference to the applicable statute is essential to allege the crime which the Indictment attempts to allege, for otherwise the Indictment would be lacking in a necessary allegation of fact. This is not true test of the sufficiency of the Indictment in the present case. The case of *Hagner v. United States,* 285 U. S. 427 sets forth the following text:

> "The true test of the sufficiency of an indictment is not whether it could have been made more definite

and certain, but whether it contains the elements of the offense intended to be charged 'and sufficiently apprises the defendant of what he must be prepared to meet . . .'"

The Federal Rules of Criminal Procedure, Rule 7, provides in part:

"(c) . . . The indictment or information shall state for each count the official or customary citation of the statute, rule, regulation or other provision of law which the defendant is alleged therein to have violated. *Error in the citation or its omission shall not be ground for dismissal* of the indictment or information . . . if the error or omission did not mislead the defendant to his prejudice." (Emphasis added.)

Assuming that there was error in the citation of the statute in the present case, the Government submits that (1) the essential elements of an offense against the United States are shown in the indictment, and (2) the appellant was not misled to his prejudice by the allegations of the indictment. The trial court, therefore, properly denied the motion to dismiss.

C. The Appellant was Classified at a Legal Meeting of the Board.

Selection Service Regulations, Section 1623.4, provides in its pertinent part:

"1623.4. Action to be Taken When Classification Determined—

(d) When the local board classifies or changes the classification of a registrant, it shall record such classification on the Classification Questionnaire (SSS Form No. 100), the Classification Record (SSS

Form No. 102), and in the space provided therefor on the face of the Cover Sheet (SSS Form No. 101)."

Selective Service Regulations, Section 1604.56, provides in its pertinent part:

"1604.56. Organization and Meetings.—. . . A majority of the members of the local board shall constitute a quorum for the transaction of business. A majority of the members present at any meeting at which a quorum is present shall decide any question or classification. Every member present, unless disqualified, shall vote on every question or classification. . . ."

Neither of the two regulations set forth above requires the signature of the Board Members present and voting on a classification to be placed on any of the records kept by the Local Board. The entries referred to by appellant in his Argument [R. p. 40] are merely the notation of classification required by Section 1623.4 of the Selective Service Regulations. There is no requirement that a member of the Local Board make this notation. The initialing of that entry by one member of the Board neither vitiates the entry itself, nor does it show the composition of the Board at the time of classification.

Further, the law presumes the Local Board has done its duty. *Koch v. United States,* 150 F. 2d 762. This presumption is not overcome by the mere initialing of an entry in the Minutes of Actions by Local Boards and Appeal Board. There was no evidence introduced by appellant that he was classified at an illegal meeting of the Local Board. His classification was valid and the trial court did not err in denying the motion for judgment of acquittal upon that ground.

D. There Was No Denial of Due Process in the Classification of the Appellant.

Appellant contends he was frustrated in his attempt to appeal his clasisfication because a clerk of the Local Board told him he had already been classified I-A-O and that the Board would not change its decision. Appellant cites several cases in which registrants were frustrated by the Local Board in some function and were thereby denied substantial rights. The present case does not parallel any of these. In the present case, the appellant received and read SSS Form 110, Notice of Classification [R. pp. 62-65]. He was then apprised of his "rights" and the procedure for obtaining them. It cannot be said from the evidence elicited at the trial that the Local Board misled the appellant either intentionally or unintentionally in the prosecution of those "rights."

Selective Service Regulations, Section 1624.1, provides in its pertinent part:

> "1624.1. Opportunity to Appear in Person—(a) Every registrant, after his classification is determined by the local board, . . . shall have an opportunity to appear in person before the . . . local board . . . if he files *a written request* therefor within 10 days after the local board has mailed a Notice of Classification (SSS Form No. 110) to him . . ." (Emphasis added.)

and Selective Service Regulation, Section 1626.11, provides in its pertinent part:

> "1626.11. How Appeal to Appeal Board Is Taken. —(a) Any person . . . may appeal . . . by filing with the local board *a written notice of appeal.*" (Emphasis added.)

The requirements of these sections are in clear language. Registrants are apprised of these requirements by SSS Form 110, Notice of Classification [Govt. Ex. 3]. This form is mailed to the registrant, notifying him of his classification by the Local Board. The appellant in the present case received such a notice. He read it. He should not now be heard to complain that he did not understand the clear and concise language of that notice. No hearing is provided by the Regulations except upon protest and *written* request. This the appellant did not do. The trial court, therefore, properly found that there was no denial of due process in the action of the clerk of the Local Board.

Assuming that the appellant's appearance could be deemed a request for a personal appearance and appeal, there is no evidence in the Record which would indicate that such request was made within the prescribed time. The only evidence on this matter was elicited from redirect examination of the appellant by his counsel and is as follows:

> "Q. Do you recall about when you went down to the local board and had this conversation with the clerk? A. It was within a few days.
>
> Q. That is all—a few days after you received that notice of clasisfication? A. Yes, sir.
>
> Mr. Tietz: That is all.
>
> The Court: How long?
>
> Mr. Tietz: I beg your pardon.
>
> The Court: How long after you had registered was it that you went down to the local board to make that appearance?
>
> The Witness: I don't remember. It was shortly after I got this card, within a week or so."

It is submitted that this evidence cannot support a claim of timely request for a personal appearance or appeal and therefore, no claim of denial of due process can be made thereon.

VI.

SUMMARY.

Appellant's classification of I-A-O by the Local Board was a valid classification made within the provisions of the regulations.

The indictment brought against the appellant properly charged an offense against the United States.

The appellant was classified I-A-O at a legal meeting of the Local Board.

There was no denial of due process in the Classification of the Appellant.

No action of the Board was arbitrary or capricious.

There was no error of law in the rulings of the trial court and therefore, the conviction should be affirmed.

Respectfully submitted,

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United States Attorney,

RAY H. KINNISON,
Assistant U. S. Attorney,
Chief of Criminal Division,

MANUEL L. REAL,
Assistant U. S. Attorney,

Attorneys for Appellee.

No. 13800

In the United States Court of Appeals

For the Ninth Circuit

ROBERT DONALD ROWLAND,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

Closing Brief of Appellant

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WESTERN PRINTING COMPANY, WHITTIER

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I.

THE DENIAL OF THE TOTAL CONSCIENTIOUS OBJECTOR STATUS AND THE DECISION TO CLASSIFY IN CLASS 1-A-O (MAKING APPELLANT LIABLE FOR NON-COMBATANT MILITARY SERVICE) WERE ARBITRARY, CAPRICIOUS AND WITHOUT BASIS IN FACT.

Appelle, arguing against appellant's above stated first point relies almost entirely on *Cox v. United States,* 332 U. S. 442.

Although appellant believes that the court is familiar with the full import of the *Cox* decision he makes

this comment: appellee overlooks that the Supreme Court unmistakably declared it to be the duty of the trial court to determine if a basis in fact existed for the final classification given; if no basis in fact existed it became the duty of the trial court to sustain a motion for a judgment of acquittal. When a trial court does not so find and the appellate court does so find then the trial court's judgment must be reversed.

Cox v. United States, 68 S. Ct. 115, 118;

Estep v. United States, 66 S. Ct. 423, 430;

Annett v. United States, ... F. 2d .....

10 C. A. Decided June 26, 1953, reversing *United States v. Annett,* 108 F. Supp. 400 because no basis in fact existed, appellant is informed by General Counsel for the Jehovah's Witnesses. Appellant promptly ordered a copy of the decision, from the Court of Appeals, and should have it for oral argument.

Neal v. United States, 203 F. 2d 111, 117;

United States v. Graham, 109 F. Supp. 377:

"Nothing appearing to contradict or impeach the verity of his claim . . . it is adjudged by this court that the classification of the defendant in 1-A is without any factual foundation." [378]

United States v. Kobil, unreported [U. S. D. Ct. E. D. Mich. #32,390 decided 9/13/51, Frank A. Picard, Judge]:

"I have searched this record. I have asked counsel to point out to me one thing that the

> board had before it besides its natural prejudices and its capacious manner—which I can understand, too, being of the type I am; it is very difficult for me to tell you what I think you ought to do and must do.
> "But it was absolutely without any basis in fact and there was no right for this draft board to classify him as 1-A. What they should have done, in my opinion, is to have made further inquiry that gave that right. There is nothing I have here to show and nothing they have that shows it if they did."

A recent decision holding that a classification contrary to all the evidence is illegal is that of Judge George B. Harris, in *United States v. Samuel Reuben Bippus,* No. 33399, Northern District of California, decided July 10, 1953. The full text is in Appendix A.

Appellee argues that the selective service system has the right to be "erroneous" and cites *Dickinson v. United States,* 203 F. 2d 336, in support. Appellant doesn't question the right of the selective service system to be "erroneous" but asserts that it can never be "illegal". A classification without basis in fact is illegal.

Dickinson does not and could not deprive an appellant of the opportunity to set up, as defenses, that he has been denied due process of law or that no basis in fact for the classification exists. Such defenses have been recognized ever since *Estep* and this doctrine was confirmed by *Cox.*

In *Dickinson* this court specifically found that a substantial basis existed for the classification. This is clearly shown on pages 343 and 344, where Dickinson's claim to a IV-D (minister's) classification, and on page 345 where his claim for a 1-O (full conscientious objector's) classification were both found to be vulnerable. If appellee had pointed out any such vulnerable spots in Rowland's selective service file, as challenged in Appellant's Opening Brief this case might be within *Dickinson*. None appearing it is within the allowable defenses authorized by *Estep* and *Cox* and a reversal is required.

Appellee closed his argument on this point with the bland statement:

> "A reading of the record in the instant case presents no circumstances which discloses any bias, prejudice or unreasonable conduct on the part of the Local Board in the classification of the appellant." [10]

Appellant makes no charges of bias or prejudice; he emphatically charges unreasonable conduct. He submits that a classification flying in the face of *all* the evidence is unreasonable because it is not based on fact.

It is noteworthy that appellee has made no attempt whatsoever to point out any pertinent evidence in the selective service file that can reasonably be said to be a "basis in fact" for the classification. In fact no evi-

dence whatsoever has been pointed out; none could have been pointed out because none exists.

When appellee, represented by experienced and learned counsel is unable to point to a single thing as a basis in fact for the classification it becomes crystal clear that the local board arbitrarily chose to compromise the claim of appellant with the board's duty to meet its quota of inductable youth. The compromise (1-A-O) was intended as a sop to the appellant and to procure an inductee for the board. The end result was unsatisfactory to both. If a basis in fact existed for the 1-A-O then prison is the correct solution; if none existed, as we submit is the truth then the district court's judgment should be reversed and the appellant be remanded to the now educated judgment of his local board until he becomes age 26.

II.

THE INDICTMENT IS FATALLY DEFECTIVE

Appellee's argument is that "(1) the essential elements of an offense against the United States are shown in the indictment, and (2) the appellant was not misled to his prejudice by the allegations of the indictment."

Appellant has never claimed he was misled but had based his complaint against the indictment on the point that no offense was charged, a point he argued fully in his Opening Brief.

III.

THE CLASSIFICATION OF APPELLANT WAS MADE AT AN ILLEGAL MEETING OF THE BOARD.

Appellee correctly argues that the regulations do not require ". . . the signature of the Board member present and voting on a classification to be placed on any of the records kept by the Local Board." [15]

If neither signatures nor the voting record had been entered in the Minutes of Actions by the Local Board and Appeal Board (Ex. p. 11) then, perhaps, the presumption of regularity would suffice to meet appellant's contention that the board meeting was illegal, although it still would seem that some record should be made to indicate the presence of a quorum and that all voted, and that the classification was by a majority vote, as required. However, that question is not present here because some of the board members *did* sign and a voting record *was* entered and on these revealing, because contradictory, facts appellant based his argument that the presumption of regularity was overcome and that further evidence, if any existed, concerning the regularity of the board meeting was required from the government.

In *Dickinson,* incidentally, the court restated an old rule evidence applicable here: ". . . if weaker and less satisfactory evidence is produced by one who might have furnished stronger and more satisfactory

proof that which he presents should be viewed with distrust." [344]

IV.

THE DEFENDANT WAS FRUSTRATED IN HIS ATTEMPT TO SECURE REVIEW AND WAS THEREBY DENIED DUE PROCESS.

Appellee contends "It cannot be said from the evidence elicited at the trial that the Local Board misled the appellant either intentionally or unintentionally in the prosecution of those 'rights'." [16]

Appellant believes that the clerk of the local board is the duly appointed and acting public contact for the board and that within the limits of the complained of action the board is bound by the callousness or stupidity of its clerk.

The timeliness of appellant's attempt to secure an appeal and a hearing before the board is of the utmost importance, of course. The timeliness of his attempt to secure a review is amply revealed by the record [R. 62] and appellant submits that the very portion quoted by appellee in his brief [17] is convincing in itself. Appellee did not seem concerned, at the time, that the testimony was either untruthful or not definite enough in fixing the time within the 10 day limitations of the regulations for no questions were asked of the witness after the judge's questions [R. 68] brought out the testimony fixing the time and that the witness be-

lieved his effort with the clerk was all the "appearance" and the "appeal" due him.

Appellant believes that the record amply shows first, that the local board clerk frustrated him and second, that he never intended to waive his right to whatever review was afforded.

Respectfully submitted,

J. B. TIETZ,
Attorney for Appellant.

Appendix

APPENDIX

(This is Judge Harris' decision referred to on page 3 herein.)

Friday, July 10, 1953

THE CLERK: The United States vs. Bippus.

MR. TIETZ: Ready for the defendant, Your Honor.

THE COURT: In the matter of Samuel Ruben Bippus, it appears that the defendant was classified 1-A by the local Draft Board and on appeal his classification sustained, after the plaintiff had been accorded a hearing by Mr. Ernest Williams. It further appears that the recommendation of both the hearing officer and the Director of Selective Service, who concurred in the classification of 1-0, were ignored by the Board. That is to say, both hearing officers and the Director of Selective Service apparently took the position that this man legitimately came within the purview of classification 1-0 providing for conscientious objectors.

The case is not without difficulty and I approach it with the natural timidity the Court has in setting aside a rule of a local Board. However, I am obliged under the circumstances and the facts as I see them to conclude that Samuel Bippus is a conscientious objector, within the authorities as I read them and within the contemplation of the rules.

The hearing before Mr. Williams discloses that the plaintiff had been a Jehovah's Witness for many years standing. His religious beliefs were so strong as to lead him to refuse to salute the Flag. His conduct resulted in his being suspended from at least two schools. Whether we regard the defendant as having fanatic zeal or with a devotion, may be ascribed. Nevertheless, his role appears to be that of a zealot within the accepted sense.

The record further reveals that the defendant served as a pioneeer in the category reserved for devoting practically full time to the ministerial work and received compensation from the witnesses themselves in the amount of $32.50 a month. The hearing officer, Mr. Williams, was apparently impressed by the sincerity and honesty and purpose of the plaintiff and apparently he believed that he voiced views of a true conscientious objector.

I feel that after such careful review by Mr. Williams, concurred in by the Director of Selective Service and in the light of observations made in this Court, that the defendant probably should have been classified as a conscientious objector and I find that the Government has failed to establish the guilt of the defendant to a moral certainty and beyond a reasonable doubt, in that the classification of 1-A made by the Draft Board and affirmed by the Appellate Board lacks evidence in its support.

Accordingly, this Court orders that the motion for a judgment of acquittal is hereby granted and the defendant is adjudicated not guilty.

MR. KARESH: I think Your Honor said the Director of Selective Service, but it should be the Department of Justice.

THE COURT: Yes, I did. The correction will be noted.

MR. TIETZ: May the bond be exonerated, Your Honor?

THE COURT: Yes.

No. 13800

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Supplemental Brief of Appellant

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On August 24, 1953 the Court ordered the parties to each file a Supplemental Brief, within 10 days, on

EXHAUSTION OF ADMINISTRATIVE PROCESS AS A PREREQUISITE TO PRESENTING A DEFENSE IN A SELECTIVE SERVICE CRIMINAL PROSECUTION.

The Court pointed out that the situation in *habeas corpus* was not comparable and expressed the desire that the situation in criminal prosecutions alone be dealt with.

I.

Falbo v. United States, 320 U. S. 549, was the Supreme Court's first expression on the point. In its decision the Court held that Falbo was in no position to defend because he had not reported at the induction station. "The connected series of steps into the national service which begins with registration with the local board does not end until the registrant is accepted by the army, navy, or civilian public service camp. Thus a board order to report is no more than a necessary intermediate step in a united and continuous process designed to raise an army speedily and efficiently.

"In this process the local board is charged in the first instance with the duty to make the classification of registrant which Congress in its complete discretion saw fit to authorize. Even if there were, as the petitioner argues, a constitutional requirement that judicial review must be available to test the validity of the decision of the local board, it is certain that Congress was not required to provide for judicial intervention *before final acceptance of an individual for national service.* The narrow question therefore presented by this case is whether Congress has authorized judicial review of the propriety of a board's classification in a criminal prosecution for wilful violation of an order *directing a registrant to report for the last step in the selective process.*" [553-554] (Italics supplied.)

[The Presiding Judge and the United States Attorney referred to Falbo as a *habeas corpus* case. They evidently had in mind *U. S. ex rel. Falbo v. Kennedy,* (C. A. 4) 141 F. 2d 689, cert. den'd. 322 U. S. 745, wherein it was held that a judgment of conviction of violating the Selective Service Act, which was affirmed by the United States Supreme Court could not be collaterally attacked on the same grounds by resort to *habeas corpus.*]

Gibson v. United States (heard with Dodez v. United States), 67 S. Ct. 301, was the next and latest selective service criminal appeal before the high court involving the point. Gibson had failed to report for work at the Civilian Public Service Camp, as ordered. Dodez reported but walked out after 5 days. The government contended that neither could defend in that Gibson had not gone far enough and that Dodez had gone too far.

"*The principal issues relate to the time of completing the administrative selective process* and the effect in each case of what was done in this respect upon the petitioner's right to make defense in the criminal proceedings on various grounds going to the validity of the classification." [302] (Italics supplied.)

The court reviewed the essential portions of the evidence and first found that a change in the regulations relative to the time and place of the physical examination removed Dodez from the scope of the *Falbo* decision.

"Dodez refused to go to the camp. But Gibson, thinking the *Falbo* decision required him to report there in order to exhaust his administrative remedies, went to the camp, remained for five days and then departed without leave. It is undisputed that he intended at no time to submit to the camp's jurisdiction or authority and that at all times made this intent clear. *Everything he did was done solely to make sure that the administrative process had been finished* and with a view to avoiding the barrier Falbo encountered in his trial when he sought to question his classification." [302] (Italics supplied.)

It is therefore evident that by "completing the administrative process" the court has consistently meant that reporting at the induction station (or the Civilian Public Service Camp) was the final step and that taking this final step gives a defendant " . . . standing in a subsequent *criminal prosecution* to challenge the validity of the classification given by his draft board." [The quoted language, with italics supplied, is that of former Attorney General McGranery in his last reported decision as a district judge: *Ex Parte Fabiani,* 105 F. Supp. 139, 145.] Rowland, the appellant in the instant case, reported at the induction station and there refused to *submit* to induction. By this conduct he avoided the barrier Falbo encountered. *Estep v. United States,* 327 U. S. 114.

II.

Rowland was not *required* to demand a personal appearance hearing at the local board and/or an appeal from its classification decision or from the reclassification decision boards must make after the personal appearance.

The appearance before the board and the appeal are optional and are privileges; an inspection of the Regulations and the official Selective Service System forms shows this. The Notice of Classification (SSS Form No. 110), at all times involved, read as follows:

> "NOTICE OF RIGHT TO APPEAL
>
> "Appeal from classification by local board must be made within 10 days after the mailing of this notice by filing a written notice of appeal with the local board.
>
> Within the same 10-day period you may file a written request for personal appearance before the local board. If this is done, the time in which you may appeal is extended to 10 days from the date of mailing of a new Notice of Classification after such personal appearance.
>
> If an appeal has been taken and you are classified by the appeal board in either Class 1-A or Class 1-A-O and one or more members of the appeal board dissented from such classification you may file a written notice of appeal to the President with your local board within 10 days after the mailing of this notice."

The Regulations pertaining to the privilege *to appear* before the local board are presently in 32 C.F.R.

§1624.1 and are similar, in all matters that concern us, to the version in effect at the time Rowland was classified. They then read:

"§624.1 [At this time the digit 1 had not been placed before the 624.1]

624.1 *Opportunity to Appear in Person.*—(a) Every registrant, after his classification is determined by the local board (except a classification which is itself determined upon an appearance before the local board under the provisions of this part), shall have an opportunity to appear in person before the member or members of the local board designated for the purpose if he files a written request therefor within 10 days after the local board has mailed a Notice of Classification (SSS Form No. 110) to him. Such 10-day period may not be extended, except when the local board finds that the registrant was unable to file such request within such period because of circumstances over which he had no control.

(b) No person other than registrant shall have the right to appear in person before the local board, but the local board may, in its discretion, permit any person to appear before it with or on behalf of a registrant: *Provided,* That if the registrant does not speak English adequately he may appear with a person to act as interpreter for him: *And provided further,* That no registrant may be represented before the local board by anyone acting as attorney or legal counsel.

(c) If the written request of the registrant to appear in person is filed after such 10-day period and the local board finds that the registrant was

unable to file such request within such period because of circumstances over which he had no control, the local board shall enter in the 'Minutes of Actions by Local Board and Appeal Board' on the Classification Questionnaire (SSS Form No. 100) the date on which the request was received and the date and the time fixed for the registrant to appear and shall promptly mail to the registrant a notice of the time and place fixed for such appearance.

(d) If such a written request of a registrant for an opportunity to appear in person is received after the 10-day period following the mailing of a Notice of Classification (SSS Form No. 110) to the registrant, the local board, unless it specifically finds that the registrant was unable to file such a request within such period because of circumstances over which he had no control, shall advise the registrant, by letter, that the time in which he is permitted to file such a request has expired, and a copy of such letter shall be placed in the registrant's file. Under such circumstances, no other record of the disposition of the registrant's request need be made.

624.2 *Appearance Before Local Board.*—(a) At the time and place fixed by the local board, the registrant may appear in person before the member or members of the local board designated for the purpose. The fact that he does appear shall be entered in the 'Minutes of Actions of Local Board and Appeal Board' on the Classification Questionnaire (SSS Form No. 100).

(b) At any such appearance, the registrant may discuss his classification, may point out the class or classes in which he thinks he should have

been placed, and may direct attention to any information in his file which he believes the local board has overlooked or to which he believes it has not given sufficient weight. The registrant may present such further information as he believes will assist the local board in determining his proper classification. Such information shall be in writing, or, if oral, shall be summarized in writing and, in either event, shall be placed in the registrant's file. The information furnished should be as concise as possible under the circumstances. The member or members of the local board before whom the registrant appears may impose such limitations upon the time which the registrant may have for his appearance as they deem necessary.

(c) After the registrant has appeared before the member or members of the local board designated for the purpose, the local board shall consider the new information which it receives and shall again classify the registrant in the same manner as if he had never before been classified.

(d) After the registrant has appeared before the member or members of the local board designated for the purpose, the local board, as soon as practicable after it again classifies the registrant, shall mail notice thereof on Notice of Classification (SSS Form No. 110) to the registrant and on Classification Advice (SSS Form No. 111) to the persons entitled to receive such notice or advice on an original classification under the provisions of section 623.4 of this chapter.

(e) Each such classification shall be followed by the same right of appeal as in the case of an original classification."

The Regulations pertaining to the privilege *to appeal* are presently in 32 C.F.R. §1626.2 and are also similar, in all matters that concern us, to the version in effect at the time Rowland was classified. They then read:

"1626.2 *Appeal by Registrant and Others.*— (a) The registrant, any person who claims to be a dependent of the registrant, any person who prior to the classification appealed from filed a written request for the current occupational deferment of the registrant, or the government appeal agent may appeal to an appeal board from any classification of a registrant by the local board except that no such person may appeal from the determination of the registrant's physical or mental condition.

(b) The government appeal agent may take any appeal authorized under paragraph (a) of this section at any time within 10 days after the date when the local board mails to the registrant a Notice of Classification (SSS Form No. 110) or at any time before the registrant is mailed an Order to Report for Induction (SSS Form No. 252).

(c) The registrant, any person who claims to be a dependent of the registrant, or any person who prior to the classification appealed from filed a written request for the current occupational deferment of the registrant, may take an appeal authorized under paragraph (a) of this section at any time within the following periods:

(1) Within 10 days after the date the local board mails to the registrant a Notice of Classification (SSS Form No. 110).

> (2) Within 30 days after the date the local board mails to the registrant a Notice of Classification (SSS Form No. 110), if, on that date, it appears that the registrant is located in one and the local board which classified the registrant is located in another of the following: The continental United States, the Territory of Alaska, the Territory of Hawaii, Puerto Rico, or the Virgin Islands of the United States."

Since appellant bases his claim on jurisdictional grounds, that is, on a void order, no appeal was necessary. The Selective Service administrative process is a continuous one beginning with registration and ending at the induction ceremony.

> *Falbo v. United States,* 320 U. S. 549;
> *Estep v. United States,* 327 U. S. 114.

The administrative process is like a ladder: the registrant must go to the very end; but there is no requirement that he step on every rung. For example, could it be contended that a Selective Service registrant has not exhausted the administrative process if he did not ask for a Personal Appearance Hearing? Yet the Personal Appearance Hearing is the only opportunity the board or any classifying official ever has to look the registrant in the eye and hear his views for deferment. In other words much if not all of the appellate procedure provided is undisputably optional; if the registrant doesn't choose to avail himself of all of it or if he is deprived of all of it or any part

of it because he is misled by Selective Service functionaries he should not be deprived of his day in court.

Even in civil cases this is true. In *Skinner & Eddy Corp. v. United States,* 39 S. Ct. 375, 377, the Interstate Commerce Commission had issued a rate order which the plaintiffs attacked as lacking statutory authority. It was there contended that plaintiff should have sought administrative review. The Court said:

> "But plaintiff does not contend that 75 cents is an unreasonable high rate, or that it is discriminatory, or that there was mere error in the action of the commission. The contention is that the commission has exceeded its statutory powers; and that, hence, the order is void. In such a case the courts have jurisdiction of suits to enjoin the enforcement of an order, even if the plaintiff has not attempted to secure redress in a proceeding before the commission."

The following cases are to the same effect:

Koepke v. Fontecchio, 177 F. 2d 125, 128 (C.A. 9);
Stark v. Wickard, 321 U. S. 288, 307-311;
Ng Fung Ho v. White, 259 U. S. 276, 284;
Gegiow v. Uhl, 239 U. S. 3, 9;
American School of Magnetic Healing v. McAnnulty, 187 U. S. 94, 107-110.

III.

Generally, where a registrant does not take any or all of the administrative remedies provided by the regulations because selective service officials frustrated or ignorantly misled him, he is excused from going through the affected remedies even if they are otherwise considered prerequisites, something we do not concede in this case.

The basis for the doctrine of exhaustion is that administrative specialists are better able than the courts to handle technical matters and the courts therefore should be relieved of such burdens. *Koepke v. Fontecchio,* 177 F. 2d 125 (C.A. 9). It was never intended that this doctrine should assist careless or ignorant officials to deprive a youngster from having his day in court.

In all the usual situations concerning exhaustion of administrative process the complainting party is an experienced business man and one who has had the benefit of legal assistance, not a youngster who actually is forbidden to have counsel at the most crucial stage of selective service procedure. [See §1624.1 (b): "No registrant may be represented before the local board by anyone acting as attorney or legal counsel."]

IV.

Reproduction of the following Regulations, in the precise form in effect when applicable to appellant, may aid the court.

1606.51 *Forms Made Part of Regulations*—(a) All forms and revisions thereof referred to in these or any new or additional regulations, or in any amendment to these or such new or additional regulations, and all forms and revisions thereof prescribed by the Director of Selective Service shall be and become a part of these regulations in the same manner as if each form, each provision therein, and each revision thereof were set forth herein in full. Whenever in any form or in the instructions printed thereon, any person shall be instructed or required to perform any act in connection therewith, such person is hereby charged with the duty of promptly and completely complying with such instruction or requirement.

(b) The Director of Selective Service, as to such persons or agencies as he designates, may waive any requirement that any form be notarized or sworn to.

625.1 *Classification Not Permanent.*—(a) No classification is permanent.

(b) Each classified registrant and each person who has filed a request for the registrant's deferment shall, within 10 days after it occurs, report to the local board in writing any fact that might result in the registrant being placed in a different classification such as, but not limited to, any change in his occupational, marital, or dependency

status, or in his physical condition. Any other person should, within 10 days after knowledge thereof, report to the local board in writing any such fact.

(c) The local board shall keep informed of the status of classified registrants. Registrants may be questioned or physically or mentally re-examined, employers may be required to furnish information, police officials or other agencies may be requested to make investigations, and other steps may be taken by the local board to keep currently informed concerning the status of classified registrants.

§1622.20 *Class IV-E: Conscientious Objector Opposed to Both Combatant and Noncombatant Training and Service.*—(a) In Class IV-E shall be placed any registrant who, by reason of religious training and belief, is found to be conscientiously opposed to participation in war in any form and to be conscientiously opposed to participation in both combatant and noncombatant training and service in the armed forces.

(b) Section 6 (j) of title I of the Selective Service Act of 1948 provides in part as follows:

> "Religious training and belief in this connection means an individual's belief in a relation to a Supreme Being involving duties superior to those arising from any human relation, but does not include essentially political, sociological, or philosophical views or a merely personal moral code."

On September 28, 1951 [Rowland was not ordered to report for induction until July 16, 1952] the follow-

ing regulations, as substitutes for the above §1622.20 (IV-E) were printed and sent to all local boards:

1622.14 *Class I-O: Conscientious Objector Available for Civilian Work Contributing to the Maintenance of the National Health, Safety, or Interest.*—(a) In Class I-O shall be placed every registrant who would have been classified in Class I-A but for the fact that he has been found, by reason of religious training and belief, to be conscientiously opposed to participation in war in any form and to be conscientiously opposed to participation in both combatant and noncombatant training and service in the armed forces.

(b) Section 6 (j) of title I of the Universal Military Training and Service Act, as amended, provides in part as follows:

> "Religious training and belief in this connection means an individual's belief in a relation to a Supreme Being involving duties superior to those arising from any human relation, but does not include essentially political, sociological, or philosophical views or a merely personal moral code."

[§1622.15 Class I-S Student Deferred by Statute] (text omitted as not relevant)

1622.16 *Class I-W: Conscientious Objector Performing Civilian Work Contributing to the Maintenance of the National Health, Safety, or Interest.*—(a) In Class I-W shall be placed any registrant who has entered upon and is performing civilian work contributing to the maintenance of

the national health, safety, or interest, in accordance with the order of the local board.

(b) In Class I-W shall be placed any registrant who subsequent to being ordered by the local board to perform civilian work contributing to the maintenance of the national health, safety, or interest has been released from such work by the local board after satisfactorily performing the work for a period of twenty-four consecutive months or has been sooner released from such work by the Director of Selective Service under the provisions of section 1660.21 of this chapter. Each such registrant shall be identified on all records by following his classification with the abbreviation "Rel." and, upon attaining an age beyond the maximum age of liability for military service under the provisions of the selective service law, all such registrants shall be reclassified in Class V-A.

Respectfully submitted,

J. B. TIETZ

Attorney for Appellant.

No. 13800

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ROBERT DONALD ROWLAND,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Supplemental Brief of Appellee.

LAUGHLIN E. WATERS,
United States Attorney,
RAY H. KINNISON,
Assistant U. S. Attorney,
Chief of Criminal Division,
MANUEL L. REAL,
Assistant U. S. Attorney,
600 Federal Building,
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TABLE OF AUTHORITIES CITED

No. 13800

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ROBERT DONALD ROWLAND,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Supplemental Brief of Appellee.

In argument of the instant case, the question was raised by this Court as to whether or not the appellant had exhausted his administrative remedies. The answer is that he had not, since he had not appealed his classification of 1-A. This raises the question of the effect of the failure to exhaust administrative remedies upon the ability of a defendant to contest a classification given by a local board upon trial for a violation of the Selective Service Act.

The Supreme Court, in the case of *Falbo v. United States,* 320 U. S. 549, considered the question of exhaustion of administrative remedies. In the *Falbo* case, *supra,* the Supreme Court affirmed the decision of the lower court refusing a defense as to the invalidity of the defendant's classification where he had not exhausted his

administrative remedies. In speaking of the question of challenging a classification upon a criminal trial without exhaustion of administrative remedies, the court says, at page 554:

> ". . . The narrow question therefore presented by this case is whether Congress has authorized judicial review of the propriety of a board's classification in a criminal prosecution for wilful violation of an order directing a registrant to report for the last step in the selective process.
>
> "We think it has not. The Act nowhere explicitly provides for such review and we have found nothing in its legislative history which indicates an intention to afford it. The circumstances under which the Act was adopted lend no support to a view which would allow litigious interruption of the process of selection which Congress created . . . Surely if Congress had intended to authorize interference with that process by intermediate challenges of orders to report, it would have said so."

In allowing attack of a classification given by a lower board, the court in the case of *Estep v. United States,* 327 U. S. 114, again seems to reiterate by dicta the position of the *Falbo* case, *supra,* by saying at page 123:

> "*Falbo v. United States, supra,* does not preclude such a defense in the present cases. In the *Falbo* case the defendant challenged the order of his local board before he had exhausted his administrative remedies. Here these registrants had pursued their administrative remedies to the end. All had been done which could be done."

Again, in *Cox v. United States,* 332 U. S. 442, the Supreme Court at page 448 reaffirmed this position in the following language:

> "Petitioners are entitled to raise the question of the validity of their Selective Service classification in this proceeding. They have exhausted their remedies in the Selective Service process and whatever their position might be in attempting to raise the question by writs of habeas corpus against the camp custodian, *they are entitled to raise the issue as a defense in a criminal prosecution for absence without leave. Gibson v. United States,* 329 U. S. 338, 351-360." (Emphasis added.)

See also *United States v. Balogh* (2d Cir.), 160 F. 2d 999.

This Court in a habeas corpus case, *Olinger, et al. v. Partridge,* 196 F. 2d 986, considered the question of exhaustion of administrative remedies in a case factually similar to the instant case. In the *Olinger* case, *supra,* the Court adopted the theory of the Supreme Court in *Falbo v. United States,* 320 U. S. 549. It is submitted that the theory of the *Olinger* case is applicable to the instant case also, and that the judgment should therefore be affirmed.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney,
RAY H. KINNISON,
Assistant U. S. Attorney,
Chief of Criminal Division,
MANUEL L. REAL,
Assistant U. S. Attorney,
Attorneys for Appellee.

No. 13803

In The

United States Court of Appeals

For the Ninth Circuit

GEORGE B. HATCHETT,

Appellant,

vs.

THE GOVERNMENT OF GUAM,

Appellee.

On Appeal from the ~~United States~~ District Court for the Territory of Guam.

APPELLEE'S PETITION FOR A REHEARING

HOWARD D. PORTER,
Attorney General,
Government of Guam,
Agana, Guam,
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TOPICAL INDEX

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No. 13803

In The

UNITED STATES COURT OF APPEALS

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GEORGE B. HATCHETT,

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THE GOVERNMENT OF GUAM,

Appellee.

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APPELLEE'S PETITION FOR A REHEARING

To the Court as Constituted in the Original Hearing of the Above Entitled Appeal, Namely: Denman, Chief Judge, and Healy and Pope, Circuit Judges:

Appellee, the Government of Guam, respectfully petitions for a rehearing in this case.

REQUIREMENT OF INDICTMENT BY GRAND JURY

1. The function of court rules is to regulate the practice of the court and to facilitate the transaction of its business. This function embraces, among other things, the regula-

tion of the forms, operation and effect of process, and the prescribing of forms, modes, and times for proceedings. But no rule of court can enlarge or restrict jurisdiction. It cannot modify substantive law.[1]

The scope, purpose and construction of the Federal Rules of Criminal Procedure[2] are set forth within the rules themselves and are as follows:

> "Rule 1. Scope — These rules govern the procedure in the courts of the United States and before United States Commissioners in all criminal proceeding, with the exceptions stated in Rule 54."
>
> *Fed. Rules Cr. Proc. rule 1,* 18 U.S.C.A.

> "Rule 2. Purpose and construction — These rules are intended to provide for the just determination of every criminal proceeding. They shall be construed to secure simplicity in procedure, fairness in administration and the elimination of unjustifiable expense and delay."
>
> *Fed. Rules Cr. Proc. rule 2,* 18 U.S.C.A.

No place is it stated in the Federal Rules of Criminal Procedure[2] that the purpose of these rules is to give the court power to enlarge or modify substantive law.

The Fifth Amendment of the Constitution of the United States reads, in part as follows:

> "No person shall be held to answer for a capital or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury. * * *"

The above excerpt from the Fifth Amendment has been repeatedly held to apply to Federal criminal cases only

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[1] *Washington-Southern Nav. Co.* v. *Baltimore & Philadelphia Steamboat Co.*, 263 U.S. 629.

[2] *Fed. Rules Cr. Proc.*, 18 U.S.C.A.

and is not a limitation on the powers of a state or a territory.[3]

A federal grand jury is a creature of statute, and may not be impaneled under any inherent power of a United States court.[4]

No study of the Organic Act of Guam[5] brings forth any provision for a grand jury for the unincorporated territory of Guam although this same Organic Act provides for and sets up a government for Guam with separation of powers into executive, legislative, and judicial. The Bill of Rights of the Organic Act of Guam is comparable to the Bill of Rights of the Constitution of the United States and it contains in Section 5, (d), (e) and (f)[6] similar provisions contained in the Fifth Amendment of the Constitution of the United States, but the provision of the Fifth Amendent relative to answering for a capital or infamous crime unless on presentment or indictment of a Grand Jury is not contained in the Bill of Rights for Guam, this provision could not have been eliminated through error, but must have been eliminated for the intentional reason that Congress did not desire Guam to have the grand jury system of in-indictment.[7] The legislature of Guam has not seen fit to

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[3] *Hawaii* v. *Mankichi*, 190 U.S. 197.
Palmer v. *Ohio*, 248 U.S. 32.
State v. *Nordstrom*, 7 Wash. 506; 164 U.S. 705.

[4] *United States* v. *Johnson*, 319 U.S. 503.

[5] The Organic Act of Guam. Public Law 630, 81st Congress, Chapter 512 as amended by Public Law 248, 82nd Congress, Chapter 655.

[6] The Organic Act of Guam, supra:

"Sec. 5 (d) No person shall be subject for the same offense to be twice put in jeopardy of punishment; nor shall he be compelled in any criminal case to be a witness against himself.

(e) No person shall be deprived of life, liberty, or property without due process of law."

(f) Private property shall not be taken for public use without just compensation."

[7] Section 5. Provides for a bill of rights granting the Guamanians protection against infringement of personal freedom. The Bill of Rights is modeled upon the United States Constitution, but does not expressly provide for trial by jury in Guam. Since Guamanians derive their tradition in law from Spain, a civil law nation, they have little knowledge or experience in trial by jury. The Guam Congress could institute trial by jury if it so desired.

United States Congressional Code, Congressional Service, 81st Congress, Second Session, Vol. 2, Legislative History, p. 2854.

enact legislation creating a grand jury system. The intent of the law making power will prevail even against the letter of the statute.[8]

The District Court of Guam has dual jurisdiction for criminal offenses arising against the United States and certain criminal offenses arising against the government of Guam. There is no direct law of the United States nor of the government of Guam which requires a person answering to a crime or to an offense against the government of Guam to answer on a presentment or indictment of a grand jury. Hatchett, the appellant in this cause, was convicted for an offense against the government of Guam. The rules of court can only be applied to that which has been created by law, the rules cannot extend the law by inference, the procedure set forth in the rules for indictment by grand jury can only apply where provisions for a grand jury have otherwise been provided for by law. There is no such law for Guam and indictment by grand jury should not be required for prosecution of capital or other infamous crimes in Guam.

SINGLE RULE OF PROCEDURE FOR DISTRICT COURT

2. The determination that a single system of procedure is to be followed in respect to all criminal cases in the District Court of Guam, those arising against the United States and those arising against the government of Guam, raises the undetermined question as to the application of the criminal rules of procedure and whether or not such opinion complies with the intent of Congress. There is no question that Congress has given to the District Court of Guam dual jurisdiction over offenses against the United States arising from the laws of the United States and offenses against the government of Guam arising from the

[8] *Hawaii* v. *Mankichi*, supra.

laws of the government of Guam[9], but Congress has likewise given to Guam an extended amount of self-government and to the legislature of Guam certain power to enact legislation.

Throughout the Federal Rules of Criminal Procedure reference is made to the term "attorney for the Government" and in Rule 54 (c), under "Application of Terms," "Attorney for the government" is determined as "the attorney general, an authorized assistant of the attorney general, a United States attorney and an authorized assistant of a United States attorney." A strict or narrow interpretation of this rule will defeat the intent of Congress in providing self-government for Guam and the right of the Guam legislature to enact legislation for the government of Guam. The legislature of Guam has provided that the Island Attorney, an official of the government of Guam appointed by the Governor of Guam, shall be the public prosecutor and conduct on behalf of the government of Guam the prosecution of all offenses against the laws of Guam which are prosecuted in the District Court of Guam.[10] The Island Attorney of Guam is not one of those persons designated in Rule 54 (c) of the Federal Rules of Criminal Procedure as "Attorney for the government."

The adoption of a single system of procedure, and this court has stated that Section 22 (b) of the Organic Act of Guam provides but a single system of procedure, namely the Federal Rules of Criminal Procedure, for the District Court of Guam and a strict interpretation thereof creates

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[9] The Organic Act of Guam. Sec. 22a, supra.

[10] Sec. 265. Appointment; deputies — The Governor of Guam shall appoint an Island Attorney and a suitable number of Deputy Island Attorneys, all of whom shall be subject to removal by the Governor.

Sec. 266. Duties generally — The Island Attorney is the public prosecutor and, by himself or a deputy, shall:

(1) Conduct on behalf of the Government of Guam the prosecution of all offenses against the laws of Guam which are prosecuted in the District Court or the Island Court and, when directed by the Attorney General, the prosecution of those offenses which are prosecuted in the Police Court.

a conflicting situation in the prosecution of criminal offenses in the District Court of Guam.

Prosecution is generally defined as the complete process of a criminal proceeding.[11] The official of the government of Guam charged with the prosecution of all offenses against the laws of Guam cannot fulfill his obligations as he is not an "attorney for the government" under the Federal Rules of Criminal Procedure, this is in violation of the intent of Congress to provide self-government for Guam as it defeats, by inference, the right of the designated official of Guam to prosecute criminal offenses in the District Court of Guam arising from the laws of Guam.

CONCLUSION

3. When rules of a court are in conflict with law, the rules must give. There is no law to support indictment by grand jury in Guam, also, provisions of the Federal Rules of Criminal Procedure are in conflict with both laws of the United States and the laws of Guam so a single rule of procedure for the District Court of Guam based on the Federal Rules of Criminal Procedure cannot apply. It was not the intent of the law making body to have indictment by grand jury in Guam nor conflict in procedure in the District Court of Guam.

REHEARING EN BANC

4. It is suggested that this case should be reheard en banc.

Respectfully submitted,

HOWARD D. PORTER,
LEON D. FLORES,
JOHN A. BOHN,
Attorneys for Appellee and Petitioner.

---

[11] *Words and Phrases.* Vol. 34, p. 624.

CERTIFICATE OF COUNSEL

I, Howard D. Porter, of counsel for appellee and petitioner above named, do hereby certify that in my judgment the foregoing petition for a rehearing is well founded, and that it is not interposed for delay.

HOWARD D. PORTER,
Attorney for Appellee
and Petitioner.

No. 13804

United States
Court of Appeals
for the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

EDWARD D. SULTAN, Respondent.

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

OLGA L. SULTAN, Respondent.

Transcript of Record

Petitions to Review Decisions of The Tax Court
of the United States

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Phillips & Van Orden Co., 870 Brannan Street, San Francisco, Calif.

No. 13804

United States
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

Stipulation of Facts—(Continued)

APPEARANCES:

For Petitioner:

MILTON CADES, Esq.,
URBAN E. WILD, Esq.,
J. RUSSELL CADES, Esq.,
EDWARD J. GREANEY, C.P.A.

For Respondent:

ROBERT G. HARLESS, Esq.

Docket No. 24513

EDWARD D. SULTAN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DOCKET ENTRIES

1949

Aug. 12—Petition received and filed, Taxpayer notified. Fee paid.

Aug. 17—Copy of petition served on General Counsel.

Aug. 12—Notice of appearance of Urban E. Wild, Milton Cades and J. Russell Cades as counsel filed.

Aug. 12—Notice of appearance of Edward J. Greaney as counsel filed.

Aug. 12—Request for Circuit hearing in Honolulu, Territory of Hawaii, filed by taxpayer. 8/31/49 Granted.

1949

Sep. 27—Answer filed by General Counsel.

Oct. 3—Copy of answer served on taxpayer, Honolulu, Territory of Hawaii.

1951

Mar. 12—Hearing set June 13, 1951, Honolulu.

May 22—Hearing changed to June 15, 1951, Honolulu.

June 19/20—Hearing had before Judge Arundell, on merits. Proceedings consolidated for hearing. Respondent's oral motion for leave to file amended answer, granted. Amended answer filed. Copies served. Stipulation of facts with exhibits 1 through 39 filed. Petitioner's brief due August 23/51. Respondent's brief due October 8/51. Petitioner's reply brief due November 23/51.

July 18—Transcript of hearing 6/19/51 filed.

Aug. 22—Brief filed by taxpayer. 8/23/51 Copy served.

Oct. 2—Motion for extension to November 7, 1951, to file brief filed by General Counsel. 10/2/51 Granted.

Oct. 22—Motion for extension to January 22, 1952, to file reply brief filed by taxpayer. 10/23/51 Granted.

Nov. 7—Reply brief filed by General Counsel.

1952

Jan. 23—Reply brief filed by taxpayer. Copy served.

1952

July 3—Findings of fact and opinion rendered, Arundell, Judge. Decision will be entered under rule 50. Copy served.

Oct. 9—Respondent's computation for entry of decision filed.

Oct. 13—Hearing set November 19, 1952, at Washington, D. C., on respondent's computation.

Oct. 30—Consent to settlement filed by taxpayer.

Oct. 31—Decision entered, Judge, Arundell, Div. 7.

1953

Jan. 19—Petition for review by U. S. Court of Appeals, Ninth Circuit, filed by General Counsel.

Feb. 6—Proof of service of petition for review on counsel filed.

Feb. 6—Affidavit of service of filing petition for review filed.

Feb. 12—Motion for extension of time to 4/17/53 to transmit record filed by General Counsel.

Feb. 13—Order extending time to 4/17/53 to prepare, transmit and deliver the record, entered.

Apr. 2—Statement of points filed by General Counsel, with statement of service by mail thereon.

Apr. 2—Statement re diminution of record filed by General Counsel, with statement of service by mail thereon.

Docket No. 24514

OLGA L. SULTAN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

[Printer's Note: Appearances and Docket Entries of No. 24514 are duplicates of Docket No. 24513.]

The Tax Court of the United States

Docket No. 24513

EDWARD D. SULTAN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IT:FC:LMJ-150D) dated April 26, 1949, and, as a basis of his proceeding, alleges as follows:

I.

The petitioner is an individual whose mailing address is 1025 Alakea Street, Honolulu, T. H. The returns here involved were filed with the Collector for the Honolulu Division.

II.

The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to petitioner on April 26, 1949.

III.

The taxes in controversy are income taxes for the years and in the amounts shown below. The deficiency asserted is $389,618.34 for the years and in the amounts shown below:

Year	Deficiency	Taxes in Controversy
1944	$145,292.17	$145,292.17
1945	183,632.00	183,632.00
1946	60,694.17	57,926.43
	$389,618.34	$386,850.60

IV.

The determination of tax set forth in said notice of deficiency is based on the following error:

1. The Commissioner of Internal Revenue has erred in holding that Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, hereinafter referred to as the "Edward D. Sultan Trust", was not, during the period February 1, 1943, to January 31, 1946, inclusive, a bona fide special partner for income tax purposes of Edward D. Sultan Co., a special partnership organized and doing business under the laws of the Territory of Hawaii;

2. The Commissioner of Internal Revenue has

erred in holding that all of the income of said Edward D. Sultan Trust during the calendar years 1944 to 1946, inclusive, is the income of petitioner for income tax purposes, subject, however, to an adjustment under the Hawaiian Community Property Law commencing as of June 1, 1945;

3. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, by adding to the income reported by petitioner for said year from said Edward D. Sultan Co., the sum of $158,396.05, being the income received by Edward D. Sultan Trust from its interest in said partnership for said partnership's fiscal year ended January 31, 1944;

4. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, by adding to the income reported by petitioner for said year the sum of $2,171.26 received by Edward D. Sultan Trust as income from dividends during the calendar year 1944;

5. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, by adding to the net gain reported by petitioner for said year the sum of $2,344.98, being the net long-term capital gain of Edward D. Sultan Trust, which was reported as income of said trust for the calendar year 1944;

6. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $145,292.17, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1944;

7. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1945, by adding to the income reported by petitioner for said year from said Edward D. Sultan Co. the sum of $203,722.46;

8. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $183,632.00, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1945;

9. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the income reported by petitioner for said year from said Edward D. Sultan Co., the sum of $73,781.83, being the income reported (less an adjustment in the amount of $29,455.74, being the amount allocable to Ogla L. Sultan, wife of petitioner, based on the Hawaiian Community Property Law in effect as of June 1, 1945) by Edward D. Sultan Trust from its interest in said partnership for said partnership's fiscal year ended December 31, 1946;

10. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of

$60,694.17, or of any part thereof, in petitioner's income tax for the taxable year ended December 31, 1946.

V.

The facts upon which petitioner relies as a basis for this proceeding are as follows:

1. The petitioner, on August 28, 1941, settled the Edward D. Sultan Trust by a transfer to Ernest Walter Sultan and Bishop Trust Company, Limited, as Trustee, of the sum of $42,000.00 under the hereinafter mentioned terms of said Trust Agreement;

2. Under the provisions of the Deed of Trust, all income of the Edward D. Sultan Trust was to be accumulated until the beneficiary, a son of petitioner, the Settlor, reached the age of twenty-one (21) years, with discretion given to the Trustees to pay out of the net income such amounts as might be necessary for the maintenance, support and education of the beneficiary, but not in excess of Three Hundred Dollars ($300.00) per month. Under the provisions of the Deed of Trust, regular payments of income were to be made to the beneficiary from the time he reached the age of twenty-one (21) years until he attains the age of thirty (30) years, at which time the trust will terminate and all the property in the trust will be turned over to the beneficiary in cash and annuities. Provisions are made for the gift over to other persons in the event of the death of the beneficiary, with the added provision that under no circumstances is any part of the income or property of the trust to go to the

Settlor. The trust is, by its terms, irrevocable, and the Settlor has no power to retake any part of the income or property of the trust, having completely parted with all incidents of ownership in the income and property of the trust;

3. By the terms of said Trust Agreement, said sum of $42,000.00 was to be invested in the purchase of a forty-two per cent (42%) interest in a special partnership to be organized under the name of "Edward D. Sultan Co.";

4. Upon application duly made in the Circuit Court of the Territory of Hawaii for approval of the said investment, after a hearing thereon an order was entered in said count under which the Trustees were instructed, authorized and directed to become a special partner in the partnership of Edward D. Sultan Co., upon compliance with the provisions of the statutes of the Territory, to make and execute a partnership agreement in the form submitted to the court, and to invest and continue to invest in the said partnership the sum of $42,-000.00 as of or on August 30, 1941;

5. Petitioner filed a gift tax return for the calendar year 1941, and paid the tax computed thereon. Thereafter, upon examination of petitioner's gift tax return, the Commissioner of Internal Revenue made a determination that, by reason of the fact that the value of the 42% interest in the partnership was greater than $42,000.00, the amount paid therefor to petitioner, petitioner was liable for ad-

ditional gift tax, which deficiency was thereupon paid by petitioner;

6. A special partnership was formed as of August 30, 1941, in the form approved by the court, between Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen, and Gabriel Lewis Sultan, general partners, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, special partner, in accordance with the special partnership law of the Territory;

7. Under the terms of the special partnership agreement, all general partners actively engaged in the business of the partnership were to receive compensation for services rendered to the partnership, which compensation was chargeable, for the purpose of computing net profits under the partnership agreement, as an expense of the business. All the remaining net profits were to be divided among all the partners in proportion to the capital investment of each of the partners. The partnership agreement contained the statutory limitations on the powers of the special partner to the effect that only the general partners had the authority to transact the business of the partnership or incur obligations or liabilities on its behalf. The special partner, at all times, could investigate the partnership affairs and advise and consult with the general partners as to its management;

8. The partnership was duly registered in the office of the Treasurer of the Territory of Hawaii, and all amendments and changes, and the final ter-

mination were so registered. As required by law, the partnership gave legal notice by publication in newspapers of general circulation of its formation, changes made therein, and, finally, of its dissolution;

9. The Trustees kept themselves fully informed of the affairs of the partnership, advised with the general partners as to the conduct of the business, received periodical statements of income, and kept a close watch on the affairs of the partnership;

10. From the time of its formation until termination of the partnership, all profits were paid out proportionately to the partners, including the special partner, and upon termination of the said partnership the trust received the full amount of its capital contribution, plus its share of all profits of the partnership to said date, in accordance with the provisions of the partnership agreement;

11. All of the property of the Edward D. Sultan Trust, under agreement between the Trustees, was held in the custody of Bishop Trust Company, Limited, one of the Trustees, which is a Hawaiian corporation duly authorized, among other things, to carry on a trust and fiduciary business, and is subject to examination by banking examiners of the office of the Treasurer of the Territory of Hawaii;

12. The Trustees have invested and reinvested the funds coming into their hands, taking title to all investments and trust property in the name of the Trustees;

13. The Trustees at no time before the beneficiary reached the age of twenty-one (21) years paid out anything for his support, maintenance or education,

and, from and after the time he reached the age of 21 years, the Trustees have paid to the beneficiary the amounts of income provided for in said Deed of Trust;

14. The gross income of said Edward D. Sultan Trust, for the taxable year 1944, included income from the partnership of Edward D. Sultan Co. in the amount of $158,396.05, which income was reported by said trust for the year 1944, the income tax was computed thereon, and said tax was properly paid by the said trust;

15. The gross income of said Edward D. Sultan Trust, for the taxable year 1944, included income from dividends in the amount of $2,171.26, which income was reported by said trust for the year 1944, the net income for income tax purposes was computed thereon by the said trust, and said tax was properly paid by the said trust;

16. The gross income of said Edward D. Sultan Trust, for the taxable year 1944, included net long-term capital gains in the amount of $2,344.98, which income was reported by said trust for the year 1944, the net income for income tax purposes was computed thereon by said trust, and said tax was properly paid by the said trust;

17. The gross income of said Edward D. Sultan Trust, for the taxable year 1945, included income from said partnership, Edward D. Sultan Co., in the amount of $203,722.46, which income was reported by said trust for the year 1945, the income tax of said trust was computed thereon, and said tax was properly paid by said trust;

18. The gross income of said Edward D. Sultan Trust, for the taxable year 1946, included income from said partnership, Edward D. Sultan Co., in the amount of $103,237.57, which income was reported by said trust for the year 1946, the income tax of said trust was computed thereon, and said tax was properly paid by said trust;

19. The Edward D. Sultan Co., a special partnership organized and doing business under the laws of the Territory of Hawaii, composed of Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen, and Gabriel Lewis Sultan, general partners, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, special partner, elected to file its tax returns on an accrual and fiscal year basis ending on the 31st day of January, and filed its first return for the fiscal year ending January 31, 1942.

Wherefore Petitioner Prays that this Court may hear the proceeding and determine that there is no deficiency due from the petitioner for the years 1944, 1945 and 1946.

/s/ EDWARD D. SULTAN,
Petitioner
MILTON CADES,
URBAN E. WILD,
J. RUSSELL CADES,
EDWARD J. GREANEY, C.P.A.,
Counsel for Petitioner

Of Counsel:
SMITH, WILD, BEEBE & CADES

Territory of Hawaii,
City and County of Honolulu—ss.

Edward D. Sultan, being duly sworn, says that he is the petitioner above named; that he has read the foregoing petition, or had the same read to him, and is familiar with the statements contained therein; that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

/s/ EDWARD D. SULTAN

Subscribed and sworn to before me this 5th day of August, 1949.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires 6-30-53.

EXHIBIT "A"

Form 1230 SN-IT-1

IT:FC:LMJ-150D April 26, 1949

Mr. Edward D. Sultan,
1025 Alakea Street, Honolulu, T. H.

Sir:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1944, December 31, 1945, and December 31, 1946, discloses a deficiency of $389,618.34 as shown in the statement attached.

In accordance with the provisions of existing in-

ternal revenue laws, notice is hereby given of the deficiency mentioned.

Within 150 days (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the 150th day) from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States at its principal address, Washington 25, D. C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P. O. Box 421, Honolulu 9, T. H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner

/s/ By H. A. PETERSON,
Internal Revenue Agent in Charge

Enclosures: Statement, Form 1276, Form of Waiver

STATEMENT

Year	Deficiency
1944	$145,292.17
1945	183,632.00
1946	60,694.17
Total	$389,618.34

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated December 4, 1947, to your protest dated June 26, 1948, and to statements made at a conference held on April 12, 1949.

A copy of this letter and statement has been mailed to your representative, Mr. Milton Cades of Smith, Wild, Beebe & Cades, P. O. Box 224, Honolulu 10, T. H., in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1944
Adjustments to Net Income

Net income as disclosed by return		$186,226.77
Unallowable deductions and additional income:		
(a) Partnership income	$158,396.05	
(b) Trust income—dividends	2,171.26	
(c) Trust income—net long-term capital gains	2,344.98	162,912.29
Total		$349,139.06

Nontaxable income and additional deductions:		
(d) Contributions	$1,033.20	
(e) Taxes	3,809.58	
(f) Other deductions	1,751.28	6,594.06
Net income adjusted		$342,545.00

Explanation of Adjustments

(a) Represents income of the partnership, Edward D. Sultan Company, reported on fiduciary return filed for the Edward D. Sultan Trust, which is held to be taxable to you.

(b) Represents dividend income of the Edward D. Sultan Trust, reported on a fiduciary return, which is held to be taxable to you.

(c) Represents net long-term capital gains of the Edward D. Sultan Trust, reported on a fiduciary return, which are held to be taxable to you.

(d) Represents contributions made by the Edward D. Sultan Company, a partnership, which were deducted on a fiduciary return filed for the Edward D. Sultan Trust. Since the income of the trust is held to be taxable to you, the contributions are deductible on your return.

(e) Represents taxes paid by the Edward D. Sultan Trust and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, the taxes are deductible on your return.

(f) Represents other deductions, mainly trustee expense, paid by the Edward D. Sultan Trust and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, the other deductions are deductible on your return.

Computation of Alternative Tax

Net income adjusted		$342,545.00
Less: Net long-term capital gains		4,088.53
Ordinary net income		$338,456.47
Less: Surtax exemptions		1,000.00
Balance (surtax net income)		$337,456.47
Surtax on $337,456.47	$281,905.39	
Ordinary net income		$338,456.47
Less, Normal tax exemption		500.00
Balance subject to normal tax		$337,956.47
Normal tax at 3% on $337,956.47	10,138.69	
Partial tax		$292,044.08
Plus: 50% of net long-term capital gains of $4,088.53		2,044.27
Alternative tax		$294,088.35

Computation of Tax

Net income adjusted		$342,545.00
Less: Surtax exemptions	1,000.00	
Surtax net income		$341,545.00

Surtax on $341,545.00		$285,625.95
Net income adjusted	$342,545.00	
Less: Normal tax exemption	500.00	
Bal. subject to normal tax	342,045.00	
Normal tax at 3% on $342,045.00		10,261.35
Total income tax		$295,887.30
Correct income tax liability		$294,088.35
Income tax liability disclosed by return, Account No. 300726		148,796.18
Deficiency in income tax		$145,292.17

Taxable Year Ended December 31, 1945

Adjustments to Net Income

Net income as disclosed by amended return		$238,829.02
Unallowable deductions and additional income:		
(a) Partnership income		203,722.46
Total		$442,551.48
Nontaxable income and additional deductions:		
(b) Contributions	$3,693.06	
(c) Taxes	2,525.92	
(d) Trustee's commission	2,150.29	
Net income adjusted		$434,182.21

Explanation of Adjustments

(a) Represents income of the partnership, Ed-

ward D. Sultan Company, reported on fiduciary return filed for the Edward D. Sultan Trust, which is held to be taxable to you. This amount consists of income transferred from the partnership return of $207,922.46, less $4,200.00 accrued salaries of the partnership, shown under "other deductions" on the fiduciary return.

(b) Represents contributions made by the Edward D. Sultan Company, a partnership, which were deducted on a fiduciary return filed for the Edward D. Sultan Trust. Since the income of the trust is held to be taxable to you, the contributions are deductible on your return.

(c) Represents taxes paid by the Edward D. Sultan Trust and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, the taxes are deductible on your return.

(d) Represents trustee's commissions paid by the Edward D. Sultan Trust and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, the trustee's commissions are deductible on your return.

Computation of Alternative Tax

Net income adjusted	$434,182.21
Less: Net long-term capital gains	1,036.20
Ordinary net income	$433,146.01
Less: Surtax exemptions	1,000.00
Balance (surtax net income)	$432,146.01

Surtax on $432,146.01	$368,072.87	
Ordinary net income		$433,146.01
Less: Normal tax exemption		500.00
Balance subject to normal tax		$432,646.01
Normal tax at 3% on $432,646.01	12,979.38	
Partial tax		$381,052.25
Plus: 50% of net long-term capital gains of $1,036.20		518.10
Alternative tax		$381,570.35

Computation of Tax

Net income adjusted	$434,182.21	
Less: Surtax exemptions	1,000.00	
Surtax net income	$433,182.21	
Surtax on $433,182.21		$369.015.81
Net income adjusted	$434,182.21	
Less: Normal-tax exemption	500.00	
Balance subject to normal tax	$433,682.21	
Normal tax at 3% on $433,682.21		13,010.47
Total income tax		$382,026.28
Correct income tax liability		$381.570.35
Income tax liability disclosed by amended return, Account No. 300591		197,938.35
Deficiency in income tax		$183,632.00

Taxable Year Ended December 31, 1946
Adjustments to Net Income

Net income as disclosed by return		$102,004.60
Unallowable deductions and additional income:		
(a) Partnership income	$73,781.83	
(b) Tidal wave loss	3,273.50	77,055.33
Total		$179,059.93
Nontaxable income and additional deductions:		
(c) Contribution	$ 2,172.88	
(d) Taxes	2,571.64	
(e) Other deductions	779.08	5,523.60
Net income adjusted		$173,536.33

Explanation of Adjustments

(a) Represents income of the partnership, Edward D. Sultan Company, reported on fiduciary return filed for the Edward D. Sultan Trust, which is held to be taxable to you. Of the total income of $103,237.57 reported by the trust, one-half of $58,911.49 earned after June 1, 1945, or $29,455.74 is allocated to Mrs. Olga L. Sultan under the Hawaii Community Property Law. The partnership reported on a fiscal year basis ending January 31, 1946.

(b) Represents one-half of the tidal wave loss on Kewalo Bay property. Since this property is considered to be the separate property of Mrs. Olga

L. Sultan, the full loss of $6,547.00 is allowable to Mrs. Sultan, and the loss deduction of $3,273.50 claimed by you is accordingly transferred to Mrs. Sultan's return.

(c) Represents contributions made by the Edward D. Sultan Company, a partnership, which were deducted on a fiduciary return filed for the Edward D. Sultan Trust. Since the income of the trust is held to be taxable to you, the contributions are deductible on your return. Of the total contribution deductions of $3,539.34 reported by the trust, one-half of $2,732.93 paid after June 1, 1945, or $1,366.56 is allocated to Mrs. Olga L. Sultan under the Hawaii Community Property Law.

(d) Represents taxes paid by the Edward D. Sultan Trust before June 1, 1945 and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, the taxes are deductible on your return.

(e) Represents other deductions, mainly trustee's commissions, paid by the Edward D. Sultan Trust, and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to you, these deductions are deductible on your return. Of the total amount of $1,108.62 deduced by the trust, one-half of $659.09 paid after June 1, 1945, or $329.54, is allocated to Mrs. Olga L. Sultan under the Hawaii Community Property Law.

Computation of Tax

Net income adjusted	$173,536.33
Less: Exemptions	1,000.00

Balance subject to tax	$172,536.33
Combined tentative normal tax and surtax on $172,536.33	$132,102.70
Less: 5% of $132,102.70	6,605.14
Correct income tax liability	$125,497.56
Income tax liability disclosed by return, Account No. 912801	64,803.39
Deficiency in income tax	$ 60,694.17

[Endorsed]: T.C.U.S. Filed Aug. 12, 1949.

[Title of Tax Court and Cause No. 24513.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the petition.

IV-1 to 10, inclusive. Denies that the Commissioner erred in the determination of the deficiencies as alleged in paragraph IV of the petition and subparagraphs 1 to 10, inclusive, thereunder.

V-1. Admits the allegations contained in subparagraph 1 of paragraph V of the petition.

2 and 3. Denies the allegations contained in subparagraphs 2 and 3 of paragraph V of the petition.

4 and 5. For lack of knowledge or information sufficient to form a belief, denies the allegations contained in subparagraphs 4 and 5 of paragraph V of the petition.

V-6 to 19, inclusive. Denies the allegations contained in subparagraphs 6 to 19, inclusive, of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
T. M. MATHER,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Sept. 27, 1949.

The Tax Court of the United States

Docket No. 24514.

OLGA L. SULTAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IT:FC:LMJ - 150D) dated April 26, 1949, and as a basis of her proceeding, alleges as follows:

I.

The petitioner is an individual whose mailing address is 1025 Alakea Street, Honolulu, T.H. The return here involved was filed with the Collector for the Honolulu Division.

II.

The notice of deficiency (a copy of which is attached and marked "Exhibit A" was mailed to petitioner on April 26, 1949.

III.

The taxes in controversy are income taxes for the year 1946 in the amount of $17,091.57. The deficiency asserted is $17,091.57, the entire amount of which is in controversy.

IV.

The determination of tax set forth in said notice of deficiency is based on the following errors:

1. The Commissioner of Internal Revenue has erred in holding that Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, hereinafter referred to as the "Edward D. Sultan Trust", was not, during the period February 1, 1945 to January 31, 1946, inclusive a bona fide special partner for income tax purposes of Edward D. Sultan Co., a special partnership organized and doing business under the laws of the Territory of Hawaii;

2. The Commissioner of Internal Revenue has erred in holding that all the income of said Edward D. Sultan Trust, during the calendar year 1946, is the income of Edward D. Sultan, husband of petitioner, for income tax purposes, and, from and after June 1, 1945, by virtue of the Hawaiian Community Property Law, one-half thereof is taxable to petitioner;

3. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the income reported by petitioner for said year from said Edward D. Sultan Co., the sum of $29,455.74 received by Edward D. Sultan trust as income from its interest in said partnership for said partnership's fiscal year ended January 31, 1946, and allocable to petitioner based

on the Hawaiian Community Property Law in effect as of June 1, 1945;

4. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $17,091.57, or of any part thereof, in petitioner's income tax for the taxable year ended December 31, 1946.

The facts upon which petitioner relies as a basis for this proceeding are as follows:

1. Edward D. Sultan, husband of petitioner, on August 28, 1941, settled the Edward D. Sultan Trust by a transfer to Ernest Walter Sultan and Bishop Trust Company, Limited, as Trustees, of a sum of $42,000.00 under the hereinafter mentioned terms of said Trust Agreement;

2. Under the provisions of the Deed of Trust, all income of the Edward D. Sultan Trust was to be accumulated until the beneficiary, a son of the Settlor, reached the age of twenty-one (21) years, with discretion given to the Trustees to pay out of the net income such amounts as might be necessary for the maintenance, support and education of the beneficiary, but not in excess of Three Hundred Dollars ($300.00) per month. Under the provisions of the Deed of Trust, regular payments of income were to be made to the beneficiary from the time he reached the age of 21 years until he attains the age of thirty (30) years, at which time the trust will terminate and all the property in the Trust will be turned over to the beneficiary in cash and annuities. Provisions are made for the gift over to other

persons in the event of the death of the beneficiary, with the added provision that under no circumstances is any part of the income or property of the trust to go to the Settlor. The trust is, by its terms, irrevocable, and the Settlor has no power to retake any part of the income or property of the trust, having completely parted with all incidents of ownership in the income and property of the trust;

3. By the terms of said Trust Agreement, said sum of $42,000.00 was to be invested in the purchase of a forty-two per cent (42%) interest in a special partnership to be organized under the name of "Edward D. Sultan Co.";

4. Upon application duly made in the Circuit Court of the Territory of Hawaii for approval of the said investment, after a hearing thereon, an order was entered in said court under which the Trustees were instructed, authorized and directed to become a special partner in the partnership of Edward D. Sultan Co., upon compliance with the provision of the statutes of the Territory, to make and execute a partnership agreement in the form submitted to the court, and to invest and continue to invest in the said partnership the sum of $42,000.00 as of or on August 30, 1941;

5. Edward D. Sultan, husband of petitioner, filed a gift tax return for the calendar year 1941, and paid the tax computed thereon. Thereafter, upon examination of the gift tax liability, the Commis-

sioner of Internal Revenue made a determination that, by reason of the fact that the value of the 42% interest in the partnership was greater than $42,000.00, the amount paid therefor to said Edward D. Sultan was liable for additional gift tax, which deficiency was thereupon paid by him;

6. A special partnership was formed as of August 30, 1941, in the form approved by the court, between Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, general partners, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, special partner, in accordance with the special partnership law of the Territory;

7. Under the terms of the special partnership agreement, all general partners actively engaged in the business of the partnership were to receive compensation for services rendered to the partnership, which compensation was chargeable, for the purpose of computing net profits under the partnership agreement, as an expense of the business. All the remaining net profits were to be divided among all the partners in proportion to the capital investment of each of the partners. The partnership agreement contained the statutory limitations on the powers of the special partner to the effect that only the general partners had the authority to transact the business of the partnership or incur obligations or liabilities on its behalf. The special partner, at all times, could investigate the partnership affairs and

advise and consult with the general partners as to its management;

8. The partnership was duly registered in the office of the Treasurer of the Territory of Hawaii, and all amendments and changes and the final termination were so registered. As required by law, the partnership gave legal notice by publication in newspapers of general circulation of its formation, changes made therein, and, finally, of its dissolution;

9. The Trustees kept themselves fully informed of the affairs of the partnership, advised with the general partners as to the conduct of the business, received periodical statements of income, and kept a close watch on the affairs of the partnership;

10. From the time of its formation until the termination of the partnership, all profits were paid out proportionately to the partners, including the special partner, and upon termination of the said partnership the trust received the full amount of its capital contribution, plus its share of all profits of the partnership to said date, in accordance with the provisions of the partnership agreement;

11. All of the property of the Edward D. Sultan Trust, under agreement between the Trustees, was held in the custody of Bishop Trust Company, Limited, one of the Trustees, which is a Hawaiian corporation duly authorized, among other things, to carry on a trust and fiduciary business, and is subject to examination by banking examiners of the office of the Treasurer of the Territory of Hawaii;

12. The Trustees have invested and reinvested

the funds coming into their hands, taking title to all investments and trust property in the name of the Trustees;

13. The Trustees, at no time before the beneficiary reached the age of 21 years, paid out anything for his support, maintenance or education, and, from and after the time he reached the age of 21 years, the Trustees have paid to the beneficiary the amounts of income provided for in said Deed of Trust;

14. The gross income of said Edward D. Sultan Trust, for the taxable year 1946, included income from said partnership in the amount of $103,237.57, which income was reported by said Trust for the year 1946, the income tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

15. The Edward D. Sultan Co., a special partnership organized and doing business under the laws of the Territory of Hawaii, composed of Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen, and Gabriel Lewis Sultan, general partners, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, special partner, elected to file its tax returns on an accrual and fiscal year basis ending on the 31st day of January, and filed its first return for the fiscal year ending January 31, 1942.

Wherefore Petitioner Prays that this Court may

hear the proceeding and determine that there is no deficiency due from the petitioner for the year 1946.

/s/ OLGA L. SULTAN,
MILTON CADES,
URBAN E. WILD
J. RUSSELL CADES,
EDWARD J. GREANERY, C.P.A.,
Counsel for Petitioner.

Of Counsel:

SMITH, WILD, BEEBE & CADES.

Territory of Hawaii,
City and County of Honolulu—ss:

Olga L. Sultan, being duly sworn, says that she is the petition above named; that she has read the foregoing petition, or had the same read to her, and is familiar with the statements contained therein; that the statements contained therein are true, except those stated to be upon information and belief, and that those she believes to be true.

/s/ OLGA L. SULTAN,

Subscribed and sworn to before me this 10th day of August, 1949.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-53.

EXHIBIT "A"

Form 1230 SN-IT-1

IT:FC:LMJ-150D

Mrs. Olga L. Sultan Apr. 26, 1949
1025 Alakea Street, Honolulu, T.H.

Madam:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1946 discloses a deficiency of $17,091.57 as shown in the statement attached.

In according with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 150 days (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the 150th day) from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States at its principal address, Washington 25, D.C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P.O. Box 421, Honolulu 9, T.H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest

period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner.
/s/ By H. A. PETERSON,
Internal Revenue Agent in Charge.

Enclosures: Statement, Form 1276 Form of Waiver.

STATEMENT

Year	Deficiency
1946	$17,091.57

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated December 4, 1947, to your protest dated June 26, 1948, and to statements made at a conference held on April 12, 1949.

A copy of this letter and statement has been mailed to your representative, Mr. Milton Cades of Smith, Wild, Beebe & Cades, P. O. Box 224, Honolulu 10, T.H., in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1946
Adjustments to Net Income

Net income as disclosed by return.....	$39,520.68
Unallowable deductions and additional income:	
(a) Partnership income	29,455.74
Total	$68,976.42

Nontaxable income and additional deductions:		
(b) Tidal wave loss	$3,273.50	
(c) Contributions	1,366.46	
(d) Other deductions	329.54	4,969.50
Net income adjusted		$64,006.92

Explanation of Adjustments

(a) Represents income of the partnership, Edward D. Sultan Company, reported on fiduciary return filed for the Edward D. Sultan Trust, which is held to be taxable to Mr. Edward D. Sultan. Of the total income of $103,237.57 reported by the trust, one-half of the $58,911.49 earned after June 1, 1945, or $29,455.74 is allocated to you under the Hawaii Community Property Law. The partnership reported on a fiscal year basis ending January 31, 1946.

(b) Represents one-half of the tidal wave loss on Kewalo Bay property which was reported on the return of Mr. Edward D. Sultan. Since the property is considered to be your separate property, the full loss of $6,547.00 is allowable to you, and the above amount claimed on Mr. Sultan's return is eliminated thereon.

(c) Represents contributions made by the Edward D. Sultan Company, a partnership, which were deducted on a fiduciary return filed for the Edward D. Sultan Trust. Since the income of the trust is held to be taxable to Mr. Edward D. Sultan, the contributions are deductible on his return. Of the

total contribution deductions of $3,539.34 reported by the trust, one-half of $2,732.93 paid after June 1, 1945, or $1,366.46, is allocated to you under the Hawaiian Community Property Law.

(d) Represents other deductions, mainly trustee's commissions, paid by the Edward D. Sultan Trust, and deducted on a fiduciary return filed for the trust. Since the income of the trust is held to be taxable to Mr. Edward D. Sultan, these deductions are deductible on his return. Of the total amount of $1,108.62 deducted by the trust, one-half of $659.09 paid after June 1, 1945, or $329.54, is allocated to you under the Hawaii Community Property Law.

Computation of Tax

Net Income adjusted	$64,006.92
Less: Exemption	500.00
Balance subject to tax	$63,506.92
Combined tentative normal tax and surtax on $63,506.92	$37,055.40
Less: 5% of $37,055.40	1,852.77
Correct income tax liability	$35,202.63
Income tax liability disclosed by return, Account No. 918429	18,111.06
Deficiency in income tax	$17,091.57

[Endorsed]: T.C.U.S. Filed Aug. 12, 1949.

[Title of Tax Court and Cause No. 24514.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the petition.

IV-1 to 4, inclusive. Denies that the Commissioner erred in the determination of the deficiency as alleged in paragraph IV of the petition and subparagraphs 1 to 4, inclusive, thereunder.

V-1. Admits the allegations contained in subparagraph 1 of paragraph V of the petition.

2 and 3. Denies the allegations contained in subparagraphs 2 and 3 of paragraph V of the petition.

4. For lack of knowledge or information sufficient to form a belief, denies the allegations contained in subparagraph 4 of paragraph V of the petition.

V-1. Admits the allegations contained in subparagraph 1 of paragraph V of the petition.

2 and 3. Denies the allegations contained in subparagraphs 2 and 3 of paragraph V of the petition.

4 and 5. For lack of knowledge or information sufficient to form a belief, denies the allegations

contained in subparagraphs 4 and 5 of paragraph V of the petition.

6 to 15, inclusive. Denies the allegations contained in subparagraphs 6 to 15 of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
T. M. MATHER,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Sept. 27, 1949.

[Title of Tax Court and Cause No. 24513.]

AMENDED ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for an amended answer to the petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraph I, II and III of the petition.

IV-1 to 10, inclusive. Denies that the Commissioner erred in the determination of the deficiencies as alleged in paragraph IV of the petition and subparagraphs 1 to 10, inclusive, thereunder.

V-1. Denies the allegations contained in subparagraph 1 of paragraph V of the petition.

2 and 3. Denies the allegations contained in subparagraphs 2 and 3 of paragraph V of the petition.

4 and 5. For lack of knowledge or information sufficient to form a belief, denies the allegations contained in subparagraphs 4 and 5 of paragraph V of the petition.

V-6 to 19, inclusive. Denies the allegations contained in subparagraphs 6 to 19, inclusive, of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
C. W. NYQUIST,
R. G. HARLESS,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed June 20, 1951.

[Title of Tax Court and Cause No. 24514.]

AMENDED ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for an amended answer to the petition filed by the above-named petitioner admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the petition.

IV-1 to 4, inclusive. Denies that the Commissioner erred in the determination of the deficiency as alleged in paragraph IV of the petition and subparagraphs 1 to 4, inclusive, thereunder.

V-1 to 3, inclusive. Denies the allegations contained in subparagraphs 1 to 3, inclusive, of paragraph V of the petition.

4 and 5. For lack of knowledge or information sufficient to form a belief, denies the allegations contained in subparagraphs 4 and 5 of paragraph V of the petition.

6 to 15, inclusive. Denies the allegations contained in subparagraphs 6 to 15, inclusive, of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
C. W. NYQUIST,
R. G. HARLESS,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed June 20, 1951.

[Title of Tax Court and Causes No. 24513-4.]

STIPULATION OF FACTS

It is Hereby Stipulated and Agreed, by and between the parties hereto, by their respective attorneys, that the following facts shall be taken as true and may be received by the Court in evidence with the same force and effect as if the facts herein contained were testified to by competent witnesses; provided, however, that this stipulation shall be without prejudice to the right of either party to introduce other or further evidence not inconsistent with the facts herein stipulated as true:

I.

That petitioners Edward D. Sultan and Olga L. Sultan are, and were at all times material to this proceeding, husband and wife and residents of the Territory of Hawaii.

II.

That petitioners have one child, Edward D. Sultan, Jr., (whose name was changed from Edward Dolph Sultan), born December 28, 1927.

III.

That petitioner, Edward D. Sultan, on August 28, 1941, created the Edward D. Sultan Trust, naming Ernest Walter Sultan and Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, as Trustees. A true copy of Trust Indenture, dated the 28th day of August, 1941, marked Exhibit 1, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

IV.

That the Trustees of the Edward D. Sultan Trust, on September 5, 1941, filed on Petition for Authority to Make Investment in the First Circuit Court of the Territory of Hawaii, being Equity No. 4245, at Chambers, in Equity, and, on September 9, 1941, Louis LeBaron Judge of said court duly entered an Order granting the request in said Petition. True copies of said Petition for Authority to Make Investment and Order, marked Exhibits 2 and 3, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

V.

That a document entitled a Special Partnership Agreement, dated the 30th day of August, 1941, was duly executed by Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, described as General Partners therein and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, described as Special Partner therein. A true copy of said Special Partnership Agreement, marked Exhibit 4, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VI.

That a Bill of Sale, dated as of the close of business on August 30, 1941, was duly executed by Edward D. Sultan, as Seller. A true copy of said Bill of Sale, marked Exhibit 5, is attached hereto, in-

corporated herein by reference, and made a part hereof for all purposes.

VII.

That on October 24, 1941, a duly executed Certificate of Special Partnership and Affidavits of Edward D. Sultan and Ernest Walter Sultan, of Marie Hilda Cohen and Gabriel Lewis Sultan, of W. A. White, and of Ernest Walter Sultan, required by Section 6875, Revised Laws of Hawaii 1935, were duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935. A true copy of said Certificate and Affidavits, marked Exhibit 6, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VIII.

That a Statement of Substance of Certificate of Special Partnership was duly published in The Honolulu Advertiser on October 31, November 3, 7 and 10, 1941.

IX.

That on or before March 15, 1942, Petitioner Edward D. Sultan filed a gift tax return for the calendar year 1941, reporting therein a gift of $42,000.00 to the Edward D. Sultan Trust. Thereafter, upon examination of said gift tax return, the Commissioner of Internal Revenue made a determination that by reason of the fact that the value of the 42% interest in the partnership, acquired by the Edward D. Sultan Trust from petitioner Edward D. Sultan,

was greater than $42,000.00, petitioner Edward D. Sultan was liable for additional gift tax in the amount of $81.99, which deficiency was thereupon paid by petitioner Edward D. Sultan.

X.

That a document entitled Amendment to Special Partnership Agreement, dated Jan. 12, 1942, was duly executed by Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, described as General Partners therein, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor, described as Special Partner therein. A true copy of said Amendment to Special Partnership Agreement, marked Exhibit 7, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XI.

That a document entitled Amendment to Special Partnership Agreement, dated June 9, 1942, was duly executed by Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, described as General Partners therein, and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor, described as Special Partner therein. A true copy of said Amendment to Special Partnership Agreement, marked Exhibit 8, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XII.

That a document entitled Amendment to Special Partnership Agreement, dated February 2, 1945, was duly executed by Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, described as General Partners therein and Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor, described as Special Partner therein. A true copy of said Amendment to Special Partnership Agreement, marked Exhibit 9, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIII.

That in January, 1949, petitioner Edward D. Sultan acquired from Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, all of their interest in Edward D. Sultan Co., and a Bill of Sale, dated the .... day of ....., 1949 (showing notarial acknowledgments of the various assignors on the 26th and 28th days of January, 1949), was duly executed by Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan. A true copy of said Bill of Sale, marked Exhibit 10, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIV.

That in a letter dated February 1, 1949, petitioner Edward D. Sultan offered to purchase from the Edward D. Sultan Trust its 42% interest in Ed-

ward D. Sultan Co. By a letter dated February 9, 1949, the offer was accepted upon approval and consent of the petitioner Edward D. Sultan, as Settlor, and Edward D. Sultan, Jr. (who had then attained his majority). True copies of letter of Edward D. Sultan to the Trustees of the Edward D. Sultan Trust dated February 1, 1949, and letter of Bishop Trust Company, Limited, to Edward D. Sultan dated February 9, 1949, marked Exhibits 11 and 12, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XV.

That in order to carry out the agreement set forth in paragraph XIV hereinabove, a Bill of Sale, dated as of the close of business on January 31, 1949, was executed by Edward D. Sultan Co., as Seller, and Edward D. Sultan, Olga L. Sultan, and Edward D. Sultan, Jr., copartners doing business under the firm name and style of Edward D. Sultan Co., as Purchaser. A true copy of said Bill of Sale, marked Exhibits 13, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XVI.

That a Statement of Dissolution of the Special Partnership of Edward D. Sultan Co. was duly filed in the Office of the Treasurer of the Territory of Hawaii on March 11, 1949. A true copy of said Statement, marked Exhibit 14, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XVII.

That Notice of Dissolution of Special Partnership of Edward D. Sultan Co. was duly published in The Honolulu Advertiser on March 12, 19, 26, and April 2, 1949.

XVIII.

That Edward D. Sultan Co. filed its partnership tax returns on an accrual and fiscal year basis ending on the 31st day of January, and filed its first return on that basis for the fiscal year ended January 31, 1942. Photostatic copies of the returns filed by Edward D. Sultan Co. for the fiscal periods ended January 31, 1942, January 31, 1943, January 31, 1944, January 31, 1945, January 31, 1946, January 31, 1947 January 31, 1948 and January 31, 1949, marked or to be marked Exhibits 15, 16, 17, 18, 19, 20, 21 and 22, are either attached hereto or will be furnished by Counsel for respondent, and incorporated herein by reference, and made a part hereof for all purposes.

XIX.

That Schedules showing the income and expenses for the period from September 1, 1941 to January 31, 1951, the payments received by the Edward D. Sultan Trust as distributions of its share of income of Edward D. Sultan Co., and the inventory of assets of the Edward D. Sultan Trust at January 31, 1951, as shown by the books and records of said Trust, marked Exhibits 23, 24 and 25, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XX.

That Edward D. Sultan Trust duly filed federal fiduciary tax returns each year and duly paid the tax shown to be due thereon. A Schedule showing the items of income and deductions, marked Exhibit 26, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes. Photostatic copies of the fiduciary tax returns filed by said Edward D. Sultan Trust for the years 1942, 1943, 1944, 1945, 1946, for the fiscal years ended Sept. 30, 1947 as originally filed and as amended, 1948, 1949 and 1950, marked or to be marked Exhibits 26, 27, 28, 29, 30, 30A, 31, 32, 33 and 34, respectively, are attached hereto or will be furnished by Counsel for respondent, incorporated herein by reference, and made a part hereof for all purposes.

XXI.

That photostatic copies of the tax returns filed by petitioner Edward D. Sultan, for the years 1944, 1945 as originally filed and as amended, and 1946, and by petitioner Olga L. Sultan, for the years 1945 and 1946, marked Exhibits 35, 36, 36A, 37, 38, and 39, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXII.

That by virtue of the Hawaiian Community Property Law, which became effective as of June 1, 1945, petitioner Olga L. Sultan, was entitled to one-half of all of the income of her husband, petitioner Edward D. Sultan, from and after that date.

XXIII.

That the entire amount of the deficiency asserted against petitioner Olga L. Sultan arises by reason of her community property interest in the income of her husband, petitioner Edward D. Sultan.

/s/ MILTON CADES,
Counsel for Petitioner,
/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

EXHIBIT No. 1

(Trust Deed—Edward S. Sultan Trust)

This indenture made this 28th day of August, 1941, by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter called the "Settlor", and Ernest W. Sultan, of Honolulu aforesaid, and Bishop Trust Company, Limited, a Hawaiian corporation, hereinafter called the "Trustees,"

Witnesseth That:

The Settlor, in consideration of the love and affection he bears for the beneficiaries and of the acceptance by the Trustees of the trust herein created, does hereby transfer, set over and deliver to the Trustees, their successors in trust and assigns, the sum of Forty-Two Thousand and No/100ths Dollars ($42,000.00) lawful money of the United States of America,

To have and to hold the same, together with all

Exhibit No. 1—(Continued)

other property which may hereafter be or become a part of the trust estate hereby created, unto the Trustees and their successors in trust, in trust, nevertheless, for the uses and purposes hereafter stated, that is to say:

(a) The Trustees shall purchase for the said sum of Forty-two Thousand and No/100ths Dollars ($42,000.00) a forty-two per cent (42%) interest in the partnership known as "Edward D. Sultan Co." a partnership duly organized and operating under that certain special partnership agreement dated August 30, 1941, and continue to a special partner in such partnership, said sum being the fair and reasonable value of said interest duly ascertained as of August 30, 1941;

(b) The Trustees shall accumulate all net income from said trust estate until Edward Dolph Sultan, son of the Settlor (born December 28, 1927) shall reach the age of twenty-one (21) years, provided, however, that the Trustees, during such time, may in their sole discretion, pay out of the net income of the said trust estate to Edward Dolph Sultan, or for his use and benefit, such amounts as may be necessary for his maintenance, support and education, but in no event shall they pay out to Edward Dolph Sultan, or for his account, any amount in excess of Three Thousand Six Hundred and No/100ths Dollars ($3,600.00) in any calendar year;

(c) The Trustees shall pay out of the net income from the said trust estate to Edward Dolph Sultan, upon his reaching the age of twenty-one (21) years

Exhibit No. 1—(Continued)

and until the termination of this trust, the sum of Three Hundred and No/100ths Dollars ($300.00) per month;

(d) The Trustees shall pay, in addition to the foregoing, one-half (½) of the accumulated net income from said trust estate but not in excess of the sum of Ten Thousand and No/100ths Dollars ($10,000.00), to Edward Dolph Sultan when he shall attain the age of twenty-five (25) years, provided, however, that in the event there is not sufficient cash included in the assets of said trust estate at the time that such payment becomes due and payable, the Trustees may satisfy this obligation by transferring, assigning and setting over to said Edward Dolph Sultan their right to receive any sums of money that may be due them as a special partner from the partnership of Edward D. Sultan Co., or any other asset owned by them as such trustees;

(e) This trust shall cease and determine at the time that Edward Dolph Sultan shall attain the age of thirty (30) years, or upon the death of said Edward Dolph Sultan, whichever event shall first occur. In the event that Edward Dolph Sultan shall attain the age of thirty (30) years, the Trustees shall thereupon transfer, set over and deliver to him the property then comprising the trust estate, together with any cash not in excess of Twenty Thousand Dollars ($20,000.00) that might then be included in the assets representing accumulated income, and any remaining balance of cash representing accumulated income shall be used by the Trus-

Exhibit No. 1—(Continued)

tees for the purchase of an annuity policy or policies in such insurance company or companies as the Trustees may designate and in such form as the Trustees may deem advisable, providing for periodic payments to said Edward Dolph Sultan during his life. In the event said Edward Dolph Sultan shall die before he attains the age of thirty (30) years then this trust shall be terminated and upon such termination the said trust estate, together with all accumulated income shall vest in Olga Linczer Sultan provided that she is still married to and living with the Settlor, or, in the event that the Settlor shall have died prior to such time, provided that the said Olga Linczer Sultan was married to and living with the Settlor at the time of his death and has not thereafter remarried, otherwise upon such termination the said trust estate, together with all accumulated income, shall vest in equal shares to those who shall survive the Settlor of his sister, Marie Hilda Cohen, of San Francisco, California, his brother, Gabriel Lewis Sultan, of said San Francisco, and his brother, Ernest Walter Sultan, and the lawful issue of any of them who shall be deceased at such time (said issue to take per stirpes and not per capita), absolutely and in fee simple;

(f) The Trustees shall receive, hold, manage and control the said trust estate, collect the income therefrom and pay all charges incident to trust estates and properly payable by said trust estate therefrom, and the Settlor authorizes the Trustees to retain, either permanently or temporarily or for such pe-

Exhibit No. 1—(Continued)

riod of time as they may deem expedient, any property conveyed, assigned or delivered to the Trustees by the Settlor of whatever nature, and the Settlor directs that the said Trustees shall not be held liable for any loss resulting to said trust estate by reason of the Trustees' retaining any such property, or for any error of judgment in this respect;

(g) The Settlor authorizes and empowers the Trustees to sell at public or private sale, convert, transfer, exchange, mortgage, hypothecate and otherwise deal in or dispose of the whole or any part of the property, real, personal or mixed, which may be from time to time a part of the trust estate, with power to accept any purchase money mortgage or mortgages for any part of the purchase or exchange price; and to invest and reinvest the whole or any part of the assets of the said trust estate, and in investing and reinvesting any assets of said trust estate the Trustees may invest in common or preferred stocks of corporations, bonds, notes, debentures, participation or investment certificates and/or in other property, real or personal, in so far as in their judgment they shall deem such investments advisable, it being the intention of the Settlor, under the foregoing provisions, to grant to the Trustees full power to invest and reinvest money in such investments as they shall deem desirable and suitable investments for trust funds without being restricted to the classes of investments which trustees are permitted by law to make, provided, however, that the Trustees shall obtain the consent of

Exhibit No. 1—(Continued)

the Settlor to make such investments during his lifetime, and provided further that in the event the Settlor shall die before the termination hereof the Trustees shall thereafter be restricted in the making of investment of trust funds to the classes of investments which trustees are permitted by law to make, except that in any event the Trustees may, without liability for any losses resulting thereform, make advances or loans to the partnership of Edward D. Sultan Co. The Settlor authorizes and empowers the Trustees, upon any increase of the capital stock of any corporation in which said trust estate shall own shares, to exercise any preemptive rights to such shares to which said trust estate may be entitled and/or to subscribe for such additional shares as in the judgment of the Trustees shall be an advisable investment; and for this purpose or for other purposes of this trust the Settlor authorizes and empowers the Trustees to borrow money, either from themselves or from others, and upon such terms and conditions as they may deem appropriate. The Trustees shall have the right and power to vote either directly or by proxy the stock of any corporation that may be a part of said trust estate from time to time at all meetings of stockholders as the Trustees may deem best;

(h) Stock dividends shall be treated as capital of the trust estate and all stock acquired by the Trustees under the exercise of rights to subscribe or the net proceeds realized by the Trustees from the sale of rights to subscribe shall be treated as capital of

Exhibit No. 1—(Continued)

the trust estate, and all other corporate distributions shall be treated as income; provided, however, that where a distribution is made through reduction of the par value of any corporate stock held by the Trustees, or, in the exclusive discretion of the Trustees, it appears to be made in or as a result of a partial or complete liquidation or dissolution of the corporation, the Trustees may in their discretion make such apportionment of any such distribution between income and capital as to them may seem just; the Trustees shall have full power and authority to decide and determine in all doubtful cases what property or moneys received by them is capital and what is income; and also, in all doubtful cases, to decide and determine what expenses and other charges are payable out of income and what out of capital; and also, in all doubtful cases, to decide and determine what proportion of payments for expenses of or charges against the trust estate are payable from income and what from capital; and all beneficiaries shall be bound by the decision and determination of the Trustees in regard to all such allocations between capital and income. The Trustees shall have authority, in their discretion, to prorate during the year and withhold from the income received by the trust estate an amount sufficient to pay proportionate shares of the expenses payable by the trust estate so that said payments of net income may be more regular and even in amount;

(i) The Settlor may transfer, convey and assign to the Trustees any property in addition to that

Exhibit No. 1—(Continued)

hereinabove referred to, to be held upon the trust hereby created, and thereafter such additional property shall be and form a part of the trust estate;

(j) The Trustees shall render annual statements of account to the persons who are the beneficiaries of this trust, as hereinabove provided, but the Trustees shall not be required to account in any court unless requested so to do by a beneficiary;

(k) If any person entitled to receive any of the income and/or capital of the trust estate shall be a minor, the Trustees may pay the share of income and/or capital to which said minor is entitled to either parent or to the natural or legally appointed guardian of such minor, and the receipt of such parent or natural or legally appointed guardian shall be a complete release, discharge and acquittance of the Trustees to account further for any payment or payments so made, and if any beneficiary is a minor, the statements of account may be furnished to either parent of or to the natural or legally appointed guardian of such minor beneficiary;

(l) Bishop Trust Company, Limited, the corporate Trustee hereunder, shall have the custody and safekeeping of all moneys and securities belonging to the trust estate which are received or collected by the Trustees. Neither Trustee hereunder shall be answerable or accountable for any act of the other Trustee in which he or it shall not participate, nor for the custody of any property except as shall come to his or its own possession or personal con-

Exhibit No. 1—(Continued)

trol, nor for any loss or damage resulting from any error of judgment or otherwise except through his or its own gross neglect or wilful default. Nor shall the Trustees or either of them be answerable or accountable for any loss or damage resulting from any act consented to by the Settlor or for any loss or damage resulting from any investment in or loan or advance to the partnership of "Edward D. Sultan Co.";

(m) In the event that Ernest W. Sultan shall be or become unable to act or shall decline to act or shall resign his office as Trustee hereunder, or from and after the death of said Ernest W. Sultan prior to the termination of the trust, then and in any of such events Marie Hilda Cohen of San Francisco, California shall be substituted as Trustee in the place and stead of said Ernest W. Sultan, and title to all property then comprising the trust estate shall be vested in Marie Hilda Cohen and Bishop Trust Company, Limited, as Trustees, without any conveyance or vesting order, and in the event that Marie Hilda Cohen shall be or become unable to act or shall decline to act or shall resign her office as Trustee hereunder, or from and after the death of said Marie Hilda Cohen prior to the termination of the trust, then and in any of such events, Bishop Trust Company, Limited, shall act as sole Trustee hereunder and title to all of the property then comprising the trust estate shall be vested in said Bishop Trust Company, Limited, as sole Trustee, without any conveyance or vesting order;

Exhibit No. 1—(Continued)

(n) It is hereby declared that this agreement shall be and is hereby made irrevocable by the Settlor, and the Settlor reserves the right to amend this instrument by adding other property to be and become a part of the estate held under the terms hereof, and the right to alter, amend, cancel or revoke any provisions of this instrument, save and except paragraph (a), (b), (c), (d) and (e) hereof; provided, however, that in no event shall any of the property or the income thereof belonging to the trust estate be paid to or inure to the benefit of the Settlor, and provided further that any amendments made by the Settlor shall be made by instrument in writing and acknowledged and filed with the Trustees and that the alteration, amendment, cancellation or revocation of any provision of this instrument shall be made only with the written consent and approval of the Trustees and of Edward Dolph Sultan after the said Edward Dolph Sultan shall have come of age;

(o) In the event that upon due application therefor in accordance with the provisions of law, the court having jurisdiction thereof does not approve of the investment by the Trustees herein of the aforesaid sum of Forty-two Thousand and No/100ths Dollars ($42,000.00) in the purchase of a forty-two per cent (42%) interest in said "Edward D. Sultan Co." and of the Trustees' continuing to be special partners in said partnership on order duly entered within sixty (60) days from the date hereof, then

Exhibit No. 1—(Continued)

this indenture shall be null and void and of no force and effect whatsoever.

The said Ernest W. Sultan and Bishop Trust Company, Limited, hereby accept the within trust and covenant and agree with the Settlor that they will faithfully discharge and carry out the same.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

/s/ EDWARD D. SULTAN,
Settlor.
/s/ ERNEST W. SULTAN.
BISHOP TRUST COMPANY,
LIMITED.
/s/ By W. A. WHITE,
Its Vice President.
/s/ By E. BENNER, Jr.
Its Asst. Vice Pres.
Trustees.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 28th day of August, 1941, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Exhibit No. 1—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 28th day of August, 1941, before me personally appeared Ernest W. Sultan, one of the Trustees mentioned in the foregoing instrument, to me known to be the person described in and who executed the foregoing instrument as Trustee and acknowledged that he executed the same as his free act and deed as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 30th day of August 1941, before me appeared W. A. White and E. Benner, Jr. to me personally known, who being by me duly sworn, did say that they are Vice-President and Assistant Vice-President, respectively of Bishop Trust Company, Limited, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said W. A. White and E. Benner Jr., acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ PHILIP H. LEVEY,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 2

In the Circuit Court of the First Judicial Circuit
Territory of Hawaii

Eq. No. 4245.

In the Matter of the Trust Estate created by Indenture of Trust dated August 28, 1941, of EDWARD D. SULTAN.

PETITION FOR AUTHORITY TO MAKE INVESTMENT

At Chambers in Equity.

To the Honorable Presiding Judge at Chambers, in Equity, of the Above Entitled Court:

Come now Ernest W. Sultan, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees of the Trust Estate created by Indenture of Trust dated August 28, 1941, of Edward D. Sultan, Petitioners herein, and show unto this Honorable Court as follows:

I.

That Petitioners are the Trustees under that certain Indenture of Trust dated August 28, 1941, made by and between Edward D. Sultan as Settlor and said Petitioners, as Trustees, a copy of which said Indenture of Trust is annexed hereto, marked Exhibit "A" and incorporated herein by reference.

II.

That Edward D. Sultan is presently engaged in the wholesale jewelry business and is operating said business at a profit, and that substantially all

Exhibit No. 2—(Continued)

of his assets and property are used in the operation of said business.

III.

That said Edward D. Sultan is desirous of encouraging his son, Edward Dolph Sultan (born December 28, 1927), to take an interest in said business when his son reaches an appropriate age therefore, and also of providing an estate for his said son which can be added to from time to time for the future care and support of said son, and for that purpose has executed the aforesaid Indenture of Trust.

IV.

That said Edward D. Sultan has agreed to and with Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan to enter into a special partnership agreement for the purpose of acquiring and thereafter conducting the business theretofore carried on by said Edward D. Sultan from and after the close of business on August 30, 1941, provided that said trust estate created by said aforementioned Indenture of Trust be a special partner thereto, owning a forty-two per cent (42%) interest in the capital thereof; that a copy of said proposed partnership agreement is annexed thereto, marked Exhibit "B" and incorporated herein by reference.

V.

That the assets and property of said Edward D. Sultan, used in the said wholesale jewelry business, having been determined as of the close of business

Exhibit No. 2—(Continued)

on August 30, 1941, to be of the net value of $100,000.00, and constituting substantially all of the assets and property of said Edward D. Sultan, are proposed to be transferred to the said special partnership.

VI.

That said Indenture of Trust provides for the transfer to the Trustees of the sum of Forty-Two Thousand Dollars ($42,000.00), which said sum is to be used by the Trustees for the purchase of a forty-two per cent (42%) interest in the partnership to be known as "Edward D. Sultan Co." and provides that said Indenture of Trust shall be null and void and of no force and effect in that event that upon due application therefor, in accordance with the provisions of law, the court of law having jurisdiction thereof does not approve of the investment by the Trustees therein of the said sum of $42,000.00 for the purchase of the 42% interest in said special partnership.

VII.

That Petitioners believe that it is for the best interest of the trust estate that the Trustees be authorized to become a special partner in the partnership of Edward D. Sultan Co. and that the Trustees be authorized to contribute, under the terms and provisions of Chapter 225, Revised Laws of Hawaii 1935, and invest in said partnership the sum of $42,000.00, together with any increase or profits required to remain in said partnership under the terms of the partnership agreement to be entered into.

Exhibit No. 2—(Continued)

Wherefore Your Petitioners Pray that this Court do authorize said Petitioners to become a special partner in the partnership of Edward D. Sultan Co. upon compliance with the terms and provisions of said Chapter 225 of the Revised Laws of Hawaii 1935; that it authorize said Petitioners as Trustees as aforesaid to make and execute a partnership agreement substantially in the form attached to this petition which is marked Exhibit "B"; and that said Petitioners be authorized to invest in the said partnership of Edward D. Sultan Co. the sum of Forty-Two Thousand Dollars ($42,000.00) for the purchase of a forty-two per cent (42%) interest in said partnership having an appraised value of One Hundred Thousand Dollars ($100,000.00) as of or on August 30, 1941, together with any increase or profits required to remain in said partnership under the terms of said partnership agreement to be entered into; and that said Petitioners may have such further instructions as may be proper in the premises.

Dated: Honolulu, T. H., this 5th day of September, 1941.

/s/ ERNEST W. SULTAN,
BISHOP TRUST COMPANY,
LIMITED,
/s/ By W. A. WHITE, Its Vice President,
/s/ By D. W. ANDERSON, Its Vice-Pres.
Trustees of the Trust Estate created by Indenture of Trust dated August 28, 1941, of Edward D. Sultan.

Exhibit No. 2—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

Ernest W. Sultan, being first duly sworn, on oath deposes and says: That he is one of the Trustees under the Indenture of Trust dated August 28, 1941, aforementioned, one of the Petitioners named in the foregoing Petition, that he has read the foregoing Petition, knows the contents thereof and that the same is true.

/s/ ERNEST W. SULTAN.

Subscribed and sworn to before me this 5th day of September, 1941.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

[Endorsed]: Filed Sept. 5, 1941.

EXHIBIT No. 3

In the Circuit Court of the First Judicial Circuit, Territory of Hawaii

Eq. No. 4245.

In the Matter of the Trust Estate created by Indenture of Trust dated August 28, 1941, of EDWARD D. SULTAN.

At Chambers, in Equity.

ORDER

The Petition of Ernest W. Sultan and Bishop Trust Company, Limited, Trustees of the Trust Estate, created by Indenture of Trust dated August 28, 1941, of Edward D. Sultan, praying that they be authorized to become a special partner in the partnership of Edward D. Sultan Co., upon compliance with the provisions of Chapter 225 of the Revised Laws of Hawaii 1935, that they be authorized as Trustees as aforesaid to make and execute a partnership agreement substantially in the form attached to the petition and marked Exhibit "B", and that they be authorized to invest in the said partnership of Edward D. Sultan Co. the sum of Forty-Two Thousand Dollars ($42,000.00) for the purchase of a forty-two per cent (42%) interest in said partnership having an appraised value of One Hundred Thousand Dollars ($100,000.00) as of or on August 30, 1941, together with any increase or profits required to remain in said partnership under the terms of the partnership agreement to

Exhibit No. 3—(Continued)

be entered into, having come on for hearing before me this 9th day of September, 1941; and

Evidence having been adduced by the Petitioners in said cause that it is to the best interest of the Trust Estate and of the beneficiaries therein that Ernest W. Sultan and Bishop Trust Company, Limited, as Trustees as aforesaid, be authorized to become a special partner in the partnership of Edward D. Sultan Co.; that the contribution of the Trustees under the terms and provisions of Chapter 225 of the Revised Laws of Hawaii, 1935 should be the amount of Forty-Two Thousand Dollars ($42,000.00); and

It appearing to the satisfaction of the Court that the prayer of the Petitioners should be granted and no good cause appearing why it should not be granted,

Now, therefore, it is hereby ordered, adjudged and decreed that Ernest W. Sultan and Bishop Trust Company, Limited, Trustees as aforesaid, be and they hereby are instructed, authorized and directed to become a special partner in the partnership of Edward D. Sultan Co. upon compliance with the provisions of Chapter 225 of the Revised Laws of Hawaii, 1935, to make and execute a partnership agreement substantially in the form attached to the Petition and marked Exhibit "B", and to invest and/or continue to invest in the said partnership of Edward D. Sultan Co. the sum of Forty-Two Thousand Dollars ($42,000.00) for the purchase of a forty-two per cent (42%) interest in

Exhibit No. 3—(Continued)

said partnership having an appraised value of One Hundred Thousand Dollars ($100,000.00 as of or on August 30, 1941, together with any increase or profits required to remain in said partnership under the terms of the partnership agreement to be entered into.

Dated: Honolulu, T.H., this 9th day of September, 1941.

[Seal] /s/ LOUIS LeBARON,
Judge of the above entitled Court,
at Chambers, in Equity.

Attest:

/s/ JAMES K. TRASK,
Clerk of the above entitled Court.

I do hereby certify that the foregoing is a full, true and correct copy of the original on file in this office.

[Seal] /s/ JAMES K. TRASK,
Clerk, Circuit Court, First Circuit
Territory of Hawaii.

[Endorsed]: Filed Sept. 9, 1941.

EXHIBIT No. 4

(Partnership Agreement—Edward D. Sultan Trust)

This Special Partnership Agreement, dated this 30th day of August, 1941, made by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, Ernest Walter Sultan, of Honolulu aforesaid, Marie Hilda Cohen of San Francisco, California, and Gabriel Lewis Sultan, of San Francisco aforesaid (hereinafter referred to as "General Partners"), and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28th, 1941, made by Edward D. Sultan, as Settlor, and recorded in the Bureau of Conveyances at Honolulu, Territory aforesaid, in Book ...., Page ....(hereinafter referred to as the "Special Partner"),

Witnesseth That:

Whereas the parties hereto, having mutual confidence in each other, do hereby form with each other a special partnership for the purpose of acquiring and thereafter conducting the business heretofore carried on by Edward D. Sultan from and after the close of business on August 30, 1941, and for other purposes as hereinafter provided, upon the following terms and conditions, that is to say:

1. Purposes: The purposes of the partnership shall be to acquire as at the close of business on August 30, 1941, all assets and to carry on the business heretofore carried on and conducted by Edward D. Sultan; to buy, sell, import, export, trade and

Exhibit No. 4—(Continued)

deal in jewelry, watches, gems, precious and semi-precious stones, and goods, wares and merchandise of every kind or nature and to engage in and carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers; to buy or otherwise acquire, own, hold, use, improve, develop, mortgage, lease or take on lease, sell, convey and in any and every other manner deal in and with and dispose of real estate, buildings and other improvements, hereditaments, easements and appurtenances of every kind in connection therewith, or any estate or interest therein of any tenure or description, to the fullest extent permitted by law, and also any and all kinds of chattels, goods, wares, merchandise and agricultural, manufacturing and mercantile products and commodities, and patents, licenses, debentures, securities, stocks, bonds, commercial paper, and other forms of assets, rights and interests and evidences of property or indebtedness, tangible, or intangible; to undertake and carry on any business investment, transaction, venture or enterprise which may lawfully be undertaken or carried on by a partnership, and any business whatsoever which may seem to the partnership convenient or suitable to be undertaken whereby directly or indirectly to promote any of its general purposes or interests or render more valuable or profitable any of its property, rights, interests or enterprises; and to acquire by purchase, lease or otherwise the property, rights, franchises, assets, business and

Exhibit No. 4—(Continued)

good will of any person, firm, association or corporation engaged in or authorized to conduct any business or undertaking which may be carried on by this partnership or possessed of any property suitable or useful for any of its own purposes and carry on the same, and undertake all or any part of the obligations and liabilities in connection therewith on such terms and conditions and for such consideration as may be agreed upon, and to pay for the same either all or partly in cash, stocks, bonds, debentures or other forms of assets or securties; and to effect any such acquisition or carry on any business authorized by this agreement either by directly engaging therein or indirectly by acquiring the shares, stocks or other securities of such other business or entity, and holding and voting the same and otherwise exercising and enjoying the rights and advantages incident thereto, and such other business as may be necessary, suitable or proper to the accomplishment of their purposes or connected or related thereto as the partners from time to time mutually may agree.

2. Name: The partnership shall be conducted and carried on under the firm name and style of Edward D. Sultan Co., and the place or places of business shall be at Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places as the partners may from time to time determine.

3. Capital: The Capital of the partnership as of the date of the commencement of the term provided

Exhibit No. 4—(Continued)

for in this agreement shall be the sum of One Hundred Thousand Dollars ($100,000.00), which amount has been determined by the appraisal of the assets transferred to the partnership as of August 30, 1941, and it is agreed that the contributions of capital of each of the partners to this agreement shall be as follows:

	Interest	Interest & %
Edward D. Sultan	$46,000.00	46%
Ernest Walter Sultan	4,000.00	4%
Marie Hilda Cohen	4,000.00	4%
Gabriel Lewis Sultan	4,000.00	4%
Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust of Edward D. Sultan, dated	42,000.00	42%

It is understand and agreed that Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees as aforesaid, shall be a Special Partner in their capacity as Trustees and not individually, and shall have all of the powers, rights and duties of special partners as prescribed by Chapter 225 of the Revised Laws of Hawaii 1935 as the same now is or as the same may from time to time be amended, and that the Special Partner shall not be liable for the debts of the partnership to any extent beyond that set forth in the provisions of Section 6887 of the Revised Laws of Hawaii 1935 as the same

Exhibit No. 4—(Continued)

now is or as the same may from time to time be amended.

4. Compensation of General Partners and Division of Profits: From time to time and as the General Parners may agree, the General Partners actively engaged in the business of the partnership shall receive as compensation for services rendered to the partnership a salary chargeable, for purposes of computing net profits hereunder, as an expense of the business, in such amount as the General Partners from time to time shall agree upon, constituting the reasonable value of the services rendered to the partnership. So long as he continues to be active in the business of the partnership, there shall be paid to said Ernest Walter Sultan, out of the net profits of the partnership, twenty-five per cent (25%) thereof. All of the remaining net profits of the partnership shall be divided for each annual period in proportion to the above stated interest of each of the partners, including the said Ernest Walter Sultan, in the original capital of the partnership, and all losses of the partnership for each annual period shall be divided among the partners in the same manner as herein provided for the division of profits. Any partner may withdraw from the partnership such portion of the profits attributable to the partner's interest as the General Partners may from time to time deem advisable. Amounts not withdrawn shall not be added to the capital account but shall be credited to advance accounts in the names of the respective partners for whom said

Exhibit No. 4—(Continued)

amounts are being held and interest at the rate of five per cent (5%) per annum computed on quarterly balances beginning as of May 1, 1942, and chargeable for the purposes of computing net profits hereunder as an expense of the business, shall be credited to said accounts.

5. Services of the Partners: General Partners, Edward D. Sultan and Ernest Walter Sultan shall diligently give their full time, attention and services to the business of the partnership and shall be faithful to the partnership in all transactions relating to said business. Neither of said General Partners shall engage in any business except that of said partnership or on account thereof and no partner shall, without the written consent of all of the partners, employ the capital or credit of the partnership in any other business than that of the partnership, and no partner shall, during the continuation of the partnership carry on or be concerned or interested directly or indirectly in any other business which is in direct competition to the business of the partnership.

6. Bankers of the Partnership: The bankers of the partnership shall be Bishop National Bank of Hawaii at Honolulu or such other bankers as the partners shall from time to time determine, and all money and money instruments received by and belonging to the partnership shall be deposited to the credit of the partnership account with the partnership bankers except that such a petty cash fund

Exhibit No. 4—(Continued)

as may be mutually agreed upon between the General Partners from time to time may be kept on hand for use in the business.

7. Limitation on Powers of Partners: The General Partners only shall have authority to transact the business of the partnership or incur obligations or liabilities. In all matters except as otherwise provided in this agreement the determination by the General Partner or Partners owning the majority in interest of the capital contributed by the General Partners shall be binding upon and shall establish the policy of the partnership. The Special Partner at all times may investigate the partnership affairs and advise the General Partners as to its management. No partner shall, without the consent of the other partners, draw, accept or assign any bill of exchange or promissory note or contract any debt on account of the partnership or employ any of the moneys or effects thereof or in any manner pledge the credit theref except in the usual and regular course of the business subject to the provisions of this agreement. No partner during the continuation of this partnership without obtaining the consent thereto of the other partners shall assume any liability for another or others by means of endorsement or by becoming guarantor, surety, or insurer, and each of the General Partners agree at all times to keep indemnified the other partners and their personal representatives and the property of the partnership against any liability for or in connection with his present and future separate debts and

Exhibit No. 4—(Continued)

engagements or actions, proceedings, claims, and demands in respect thereof.

8. Partners not to Assign Interest: No General Partner shall assign or mortage his or her share of or interest in or any part of the share of or interest in the partnership or the assets or profits thereof, Provided, however, that any partner may purchase all or any part of the interest of any other partner. Additional capital contributions resulting in a change in the percentage of interest of any partner, or loans or advances to the partnership on which interest is to be computed and charged, for the purpose of computing net profits hereunder as an expense of the business, may only be made with the approval of the General Partner or Partners owning the majority in interest of the capital of the partnership; provided, however, that in the event any partner shall make additional capital contributions to the partnership the other partners shall have the right to make similar contributions in order to keep the interest of each partner in the partnership in proportions equal to those in existence at the date of the inception of the partnership. The Special Partner may assign its share or interest in the partnership only with the consent of the General Partners evidenced by written consent attached to such assignment and filed in the office of the partnership, and the General Partners shall have full power and discretion to give or withhold such consent.

9. Books of Account and Access Thereto: Proper

Exhibit No. 4—(Continued)

partnership books of account shall be kept by the partners and entry shall be made therein of all transactions and all such matters and things as usually are entered in books of account kept by persons engaged in the same or similar businesses. Such books of account and all documents, letters, papers, instruments, and records belonging to the partnership shall be kept at the office of the partnership and each partner at all times shall have full and free access to examine and copy the same. The books of the partnership may be audited periodically at such times as the partners shall determine and copies of the auditor's report shall be delivered to each partner; and in such audit the capital accounts and the advance accounts of the partners and of each partner shall be stated as at the end of each quarter-annual period.

10. Annual Account: A general account shall be taken annually of the assets and liabilities of the partnership, of all dealings and transactions of the same during the then preceding year, of all matters and things usually included in accounts of a like nature taken by persons engaged in like businesses, and in taking such account a just valuation shall be made of all items requiring valuation, and such annual account shall state the capital of the partnership and the interest of each partner therein at the end of the period of the accounting, such general account to be sent to each partner, and unless within three (3) months any partner shall ob-

Exhibit No. 4—(Continued)

ject to the same, the same shall be binding upon the partners, except for manifest errors or fraud.

11. Determination of Partnership: The partnership may be determined by a majority in interest of the General Partners at any time upon giving not less than two (2) months' previous notice in writing to the other partners of the intention of the majority of the General Partners in that behalf; and at the expiration of such notice the partnership shall determine accordingly. The term "majority in interest of the General Partners" shall mean any one or more of the General Partners, the aggregate of whose capital account as shown by the books of the partnership shall be in excess of fifty per cent (50%) of the total capital interest of all of the General Partners of the Partnership. Upon the determination of the partnership from whatever cause the General Partners agree that they will make a true, just and final account of all things relating to said business and in all things duly adjust the same. After the affairs of the partnership are adjusted, its debts paid and discharged, and the expense of liquidation shall have been paid, all the balance then remaining shall be applied first in payment to each partner or his or her representative of the balance due to each partner as shown in the advance account of said partner, then in payment of his or her share of the capital as shown on the books of the partnership as of the close of business of the partnership, and the balance shall be divided in the

Exhibit No. 4—(Continued)

same manner as hereinbefore provided for the division of profits. In the event that the balance remaining after the payment of said debts and expenses and the balances due to each partner is insufficient to pay in full the capital accounts of all of the partners, then such balance shall be applied first in payment to the Special Partner of its share of the capital as shown on the books of the partnership as at the close of business of the partnership and the balance shall be paid to each General Partner in proportion to his or her capital shown on the books of account of the partnership as of the close of business of the partnership, and, in the event the balance remaining after the payment of said debts and expenses is insufficient to pay in full the balance due to each partner as shown in the advance account of said partner, then the amounts shown as due to the Special Partner shall be paid first, the share of the capital of the Special Partner as shown on the books of the partnership shall be paid next, and the remaining balance, if any, shall be prorated among the General Partners according to the respective amounts shown on the books to be due in the advance account of each of said partners. The partners or their representatives shall execute such instruments for facilitating and effecting the realization and the division of the assets of the partners and for their mutual indemnity and release and otherwise as may be requisite or proper.

Exhibit No. 4—(Continued)

12. Death of General Partner Edward D. Sultan: If General Partner Edward D. Sultan shall die before the expiration of the partnership, his representative shall have the option (such option to be declared by notice in writing given to the surviving partners or left at the office of the partnership within six (6) calendar months after his death), of succeeding to or carrying on the interest of the deceased partner in said business either as a General Partner, in accordance with law, or as a Special Partner, under the provisions of Chapter 225, Revised Laws of Hawaii 1935, as the same now is or as the same may from time to time be amended; and if such option shall be exercised the said business shall be carried on during the residue of said term as from the death of said Edward D. Sultan as nearly as may be according to the provisions of these presents, but so that the representative of said Edward D. Sultan shall succeed to his share in said business and be substituted for him as a dormant General Partner or as a Special Partner; provided that in the case the representative of said Edward D. Sultan shall elect to become a dormant General Partner or a Special Partner by virtue of such option as aforesaid, all proper instruments for carrying out the provisions of this present clause shall be executed and made between the representative and the surviving partners, and all proper notices, publications, petitions or court proceedings shall be made and executed or taken at the expense of the partnership.

Exhibit No. 4—(Continued)

13. Option to Purchase Share of Deceased Partner or of General Partner Desiring to Terminate Partnership: In the event of the death of any General Partner other than Edward D. Sultan, or of the giving of notice to terminate the partnership by any General Partner other than Edward D. Sultan, the said Edward D. Sultan shall have the option (to be exercised by notice in writing given to the Executor or Administrator, if any, or if none then left at the office of the partnership, or by notice in writing to the General Partner giving such notice to terminate the partnership and leaving a copy of said notice at the office of said partnership within six (6) calendar months after the death of such General Partner or of the giving of the notice to terminate the partnership, as the case may be), to purchase the interest in the partnership of such deceased General Partner, or of such General Partner giving notice to terminate the partnership, for an amount equivalent to the fair value thereof as determined by an auditor or auditors of the partnership or by the value of the interest as shown on the books of account of the partnership, whichever amount is less. In determining the fair value of such interest, no value shall be attributable to good will. If said Edward D. Sultan shall exercise his option and the purchase is consummated, the same shall be considered as effective on the date when the option was exercised and the estate of such deceased partner shall not be entitled to receive any share of the net profits from and after said date

Exhibit No. 4—(Continued)

but shall be entitled to receive interest at the current bank rate upon the amount to be paid for the deceased partner's interest from said date. Said Edward D. Sultan shall have the right to make payments therefor at such time or times not later than five (5) years after the date when the said option to purchase the deceased partner's interest was exercised as he may deem advisable.

14. Winding up on Death of General Partner: In case the representative of said Edward D. Sultan shall not exercise his option to succeed to the deceased partner's share in said business as a General or a Special Partner, and in the event of the death of any other General Partner except said Edward D. Sultan, the said Edward D. Sultan shall not purchase the interest of said deceased General Partner, then the partnership shall be wound up at the expiration of six (6) calendar months from the date of such death or such sooner time as the surviving General Partners and the representatives of the deceased General Partner may agree upon and its affairs settled in the manner provided in Paragraph 11 hereof.

15. Bankruptcy, etc.: If any of the General Partners shall at any time during the partnership become incapacitated, bankrupt, insolvent, or enter into any composition or arrangement with or for the benefit of his or her creditors, or commit any breach of any of the stipulations or agreements herein contained, the other General Partners may

Exhibit No. 4—(Continued)

determine the partnership so far as such last mentioned General Partner is concerned by giving notice in writing, left at the office of the partnership, to the partner becoming incapacitated, bankrupt, insolvent, or entering into such composition or arrangement, or committing such breach, and may publish notice of dissolution of the partnership in regard to such last mentioned General Partner, without prejudice to the remedies of the other General Partners for any antecedent breach of any of the stipulations or agreements aforesaid.

16. Arbitration: If at any time during the continuance of the partnership or after the dissolution or determination thereof any dispute, difference or question shall arise between the partners or their representatives touching the partnership or the accounts or transactions thereof or the dissolution or winding up thereof or the construction, meaning, or effect of these presents or anything herein contained, or the rights or liabilities of the partners or their representatives under these presents or otherwise in relation to the premises, then every such dispute, difference or question shall, at the desire of any partner, be submitted to and determined by three (3) arbitrators, in the manner provided by Chapter 116, Revised Laws of Hawaii 1935, as the same now is or may from time to time be amended, in which case any partner may give to the other partners written notice of a desire to have an arbitration of the matter in dispute and name one of the arbitrators in said written notice, whereupon the other

Exhibit No. 4—(Continued)

partners within ten (10) days after the receipt of such notice shall name a second arbitrator, and in case of failure to do so the arbitrator already appointed shall name such second arbitrator, and the two arbitrators so appointed (in either manner) shall select and appoint the third arbitrator, and in the event that any two arbitrators so appointed shall fail to appoint a third arbitrator within ten (10) days after the naming of the second arbitrator, any party may have the third arbitrator selected or appointed by the person being the Chief Justice of the Supreme Court of the Territory of Hawaii, holding office at that time, and the three arbitrators so appointed shall thereupon proceed to determine the matter in question, disagreement or difference, and the decision of any two of them (including the disposition of the costs of arbitration) shall be final, conclusive, and binding upon all parties, unless the same shall be vacated, modified, or corrected as by said statute provided. The arbitrators shall have all the powers and duties prescribed by said statute and judgment may be entered upon any such award by the Circuit Court of the First Judicial Circuit as provided in said statute.

17. Amendments: If at any time during the continuance of this partnership the parties hereto shall deem it necessary or expedient to make any alteration in any article, clause, matter or thing herein contained for the more advantageous or satisfactory

Exhibit No. 4—(Continued)

management of the partnership business, it shall be lawful for them so to do by any writing under their joint hands, endorsed on these articles or entered in any of the partnership books, and all such alterations shall be adhered to and have the same effect from and after the time of the adoption of the same as if the same had originally been embodied in and formed a part of these presents.

18. Term of Partnership: The term of the partnership shall be for a period commencing with the date of execution hereof and ending April 30, 1943, and subject to the provisions of Paragraph 11 hereinabove, shall continue from year to year, ending April 30th of each year, thereafter until terminated by any General Partner by the giving of not less than six (6) months' written notice of his or her intention to terminate the partnership, by leaving the same at the office of the partnership.

19. Definitions: The term "General Partner" as used herein shall include the heirs, executors, administrators and permitted assigns of the General Partners, and the term "Special Partner" as used herein shall include the said Bishop Trust Company, Limited, and Ernest Walter Sultan, in their capacity as Trustees under Deed of Trust of Edward D. Sultan, dated August 28th, 1941, and not in their individual capacity, and their successors in trust and assigns.

In Witness Whereof the parties hereto have exe-

Exhibit No. 4—(Continued)

cuted these presents as of the day and year first above written.

[Seal] /s/ EDWARD D. SULTAN,
/s/ ERNEST WALTER SULTAN,
/s/ MARIE HILDA COHEN,
/s/ GABRIEL LEWIS SULTAN,
General Partners.

/s/ ERNEST WALTER SULTAN,
BISHOP TRUST COMPANY,
LIMITED,
/s/ By W. A. WHITE, Its Vice-President
/s/ By E. BENNER, Jr., Its Asst. Vice-Pres.
Trustees under Deed of Trust of Edward D. Sultan. Dated August 28th, 1941, and not individually, Special Partner.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 12th day of September, 1941, before me appeared W. A. White and E. Benner, Jr., to me personally known, who being by me duly sworn, did say that they are Vice President and Assistant Vice President, respectively of Bishop Trust Company, Limited, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28th, 1941, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors

Exhibit No. 4—(Continued)

and said W. A. White and E. Benner, Jr. acknowledged said instrument to be the free act and deed of said corporation, as such Co-Trustee.

[Seal] /s/ KENNETH DREWLINER,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission Expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 28th day of August, 1941, before me personally appeared Edward D. Sultan and Ernest Walter Sultan, to me known to be the persons described in and who executed the foregoing instrument, and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 28th day of August, 1941, before me personally appeared Ernest Walter Sultan, one of the Trustees mentioned in the foregoing instrument, to me known to be the person described in and who executed the foregoing instrument as Trustee and acknowledged that he executed the same as his free act and deed as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Exhibit No. 4—(Continued)

State of California,
City and County of San Francisco—ss:

On this 3rd day of September, 1941, before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ MARK E. LEVY,
Notary Public in and for the City and County of San Francisco, State of California. My Commission expires September 28th, 1943.

State of California,
City and County of San Francisco—ss.

On this 3rd day of September, 1941, before me personally appeared Gabriel Lewis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARK E. LEVY,
Notary Public in and for the City and County of San Francisco, State of California. My Commission expires September 28th, 1943.

EXHIBIT No. 5

This indenture, made as of the close of business on August 30, 1941, by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter called the "Seller" and Edward D. Sultan Co., a Special Partnership composed of Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, as General Partners, and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor, as Special Partner, havings its principal place of business in Honolulu aforesaid, hereinafter called the "Partnership,"

Witnesseth That:

The Seller, for and in consideration of the transfer to him of those certain promissory notes payable on demand and made by him on August 28, 1941, to the order of Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor, in the amount of Forty-Two Thousand and No/100ths Dollars ($42,000.00) to the order of Ernest Walter Sultan, in the amount of Four Thousand and No/100ths Dollars ($4,000.00), to the order of Marie Hilda Cohen in the amount of Four Thousand and No/100ths Dollars ($4,000.00), and to the order of Gabriel Lewis Sultan in the amount of Four Thousand and No/100ths Dollars ($4,000.00),

Exhibit No. 5—(Continued)

and the transfer to him of a Forty-Six Per Cent (46%) interest in the capital of the partnership, does hereby grant, bargain, sell, assign, transfer, set over, confirm and deliver unto the Partnership, its successors and assigns, forever, all and singular, the rights, property, assets, privileges and business formerly carried on by him, of the value of One Hundred Thousand Dollars ($100,000.00) as shown on the balance sheet prepared by Tennent & Greaney, dated as of the close of business August 30, 1941, including particularly but without in any wise limiting the generality of the foregoing, all chattels, leaseholds, machines and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, books, accounts, inventories, together with all other personal property, goods and chattels, of every kind and description, wheresoever situate, all good will, trade names, trade connections, licenses and all contracts and agreements including any and all rights under policies of indemnity, fidelity or other bonds or insurance of any and every kind, all cash on hand or in bank or banks, bonds, mortgages, conditional sales agreements, accounts and bills receivable, promissory notes, claims, demands, equities and choses in action and all other property and assets, tangible or intangible, of every kind or nature, owned or claimed by the Seller and used by him in the business now carried on and shown on said balance sheet; save and exept the consideration received by

Exhibit No. 5—(Continued)

him from the Partnership as the purchase price for the foregoing,

To have and to hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits and appurtenances to the same or any part thereof belonging or appertaining or held and enjoyed therewith, unto the Partnership, its successors and assigns, absolutely and forever, or in fee simple, as the case may be;

And for the consideration aforesaid the Seller does hereby irrevocably appoint the Partnership, its successors and assigns, his true and lawful attorney, in his name, place and stead to ask, demand, sue for and recover any and all moneys, assets or other property conveyed and transferred hereby or intended so to be, and the rights and benefits thereof; and does further covenant that he, the Seller, will at any time at the request of the Partnership make, execute, and deliver all such receipts, powers of attorney, and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property, claims or demands hereinabove conveyed and assigned or intended so to be as the Partnership reasonably may require.

In Witness Whereof the Seller has executed these presents as of the close of business August 30, 1941.

/s/ EDWARD D. SULTAN.

Exhibit No. 5—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 13th day of September, 1941, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 6

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of EDWARD D. SULTAN CO.

CERTIFICATE OF SPECIAL PARTNERSHIP

The undersigned, being desirous of forming a special partnership hereby certify in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935, as follows:

1. The name under which the partnership is to be conducted is "Edward D. Sultan Co.";

2. The general nature of the business intended to be transacted is to buy, sell, import, export, trade and deal in jewelry, watches, gems, precious and semi-precious stones and goods, wares and merchandise of every kind and nature, and to carry on the

Exhibit No. 6—(Continued)

business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is 1025 Alakea Street, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places in the Territory of Hawaii as the partners from time to time shall determine;

3. The names of the partners and the residence of each are as follows:

Edward D. Sultan, General Partner, Honolulu, T.H.

Ernest Walter Sultan, General Partner, Honolulu, T.H.

Marie Hilda Cohen, General Partner, San Francisco, California.

Gabriel Lewis Sultan, General Partner San Francisco, California.

Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, Special Partner, Honolulu, T.H.

4. The amount of capital which the Special Partner has contributed to the special partnership assets is $42,000.00;

5. The term for which the partnership is to exist commenced on August 30, 1941, and will continue until April 30, 1943, and thereafter from year to

Exhibit No. 6—(Continued)

year until terminated as provided in that certain Special Partnership Agreement dated August 30, 1941.

In Witness Whereof the undersigned have caused this certificate to be executed this 13th day of September, 1941.

/s/ EDWARD D. SULTAN,
/s/ ERNEST WALTER SULTAN,
/s/ MARIE HILDA COHEN,
/s/ GABRIEL LEWIS SULTAN,
/s/ ERNEST WALTER SULTAN, and
BISHOP TRUST COMPANY,
LIMITED,
Trustees as aforesaid,

[Seal] /s/ W. A. WHITE,
Its Vice-President.

/s/ D. W. ANDERSON,
Its Asst. Vice-Pres.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 30th day of September, 1941, before me appeared W. A. White and D. W. Anderson, to me personally known, who, being by me duly sworn, did say that they are Vice President and Assistant Vice President respectively of Bishop Trust Company, Limited, a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and D. W. Anderson

Exhibit No. 6—(Continued)

acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission Expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 13th day of September, 1941, before me personally appeared Edward D. Sultan and Ernest Walter Sultan, to me known to be the persons described in and who executed the foregoing instrument, and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 13th day of September, 1941, before me personally appeared Ernest Walter Sultan, one of the Trustees mentioned in the foregoing instrument, to me known to be the person described in and who executed the foregoing instrument as Trustee and acknowledged that he executed the same as his free act and deed as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Exhibit No. 6—(Continued)

State of California,
City and County of San Francisco—ss:

On this 24th day of September, 1941, before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ MARK E. LEVY,

Notary Public in and for the City and County of San Francisco, State of California. My commission expires September 28th, 1943.

State of California,
City and County of San Francisco—ss:

On this 24th day of September, 1941, before me personally appeared Gabriel Lewis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARK E. LEVY,

Notary Public in and for the City and County of San Francisco, State of California. My commission expires September 28th, 1943.

State of California,
City and County of San Francisco—ss:

I, H. A. van der Zee, County Clerk of the City and County of San Francisco, State of California, and ex-officio Clerk of the Superior Court thereof (the same being a Court of Record, having by law

Exhibit No. 6—(Continued)

a seal), being the officer authorized by the laws of said State of California to make the following certificate, do hereby certify: That Mark E. Levy whose name is subscribed to the Jurat, Affidavit, or Certificate of the Proof or Acknowledgment of the annexed instrument, was, at the time of taking the same, a Notary Public in and for said City and County of San Francisco, residing therein, duly commissioned, qualified and sworn and duly authorized by the laws of said State of California to take Jurats, Affidavits, and the Acknowledgments and Proofs of Deeds or conveyances for lands, tenements or hereditaments in said State, to be recorded therein.

I further certify that I am well acquainted with the handwriting of said Notary Public and verily believe that the signature to said Jurat, Affidavit, Acknowledgment or Certificate is genuine, and that the said instrument is executed or acknowledged according to the laws of said State of California. Further that I have compared the impression of the seal affixed thereto with a specimen impression thereof deposited in my office pursuant to law, and that I believe the impression of the seal upon the original certificate is genuine.

In testimony whereof, I have hereunto set my hand and affixed the seal of said Superior Court.

Dated: Sept. 25, 1941.

[Seal] /s/ H. A. VAN DER ZEE, Clerk.

Exhibit No. 6—(Continued)

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935.

Territory of Hawaii,
City and County of Honolulu—ss:

Edward D. Sultan and Ernest Walter Sultan, being first duly sworn, on oath each for himself doth depose and say:

That they are residents of Honolulu, City and County of Honolulu, Territory of Hawaii; that Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, is a Special Partner in the partnership of Edward D. Sultan Co.; that as Special Partner said Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees as aforesaid, actually have paid into the partnership as a capital contribution the sum of $42,000.00 in lawful money;

And further affiants sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ EDWARD D. SULTAN,

/s/ ERNEST WALTER SULTAN,

Exhibit No. 6—(Continued)

Subscribed and sworn to before me this 13th day of September, 1941.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935.

State of California
City and County of San Francisco—ss:

Marie Hilda Cohen and Gabriel Lewis Sultan, being first duly sworn, on oath each for herself and himself doth depose and say:

That they each are residents of San Francisco, California; that they each are a General Partner in the partnership of Edward D. Sultan Co.; that Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, is a Special Partner in the partnership of Edward D. Sultan Co.; that as Special Partner said Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees aforesaid, actually have paid into the partnership as a capital contribution the sum of $42,000 in lawful money;

And further affiants sayeth not except that this Affidavit is made in accordance with the require-

Exhibit No. 6—(Continued)

ments of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ MARIE HILDA COHEN,
/s/ GABRIEL LEWIS SULTAN.

Subscribed and sworn to before me this 24th day of Spetmber, 1941.

[Seal] /s/ MARK E. LEVY,

Notary Public in and for the City and County of San Francisco, State of California. My Commission expires September 28th, 1943.

State of California,
City and County of San Francisco—ss:

I, H. A. van der Zee, County Clerk of the City and County of San Francisco, State of California, and ex-officio Clerk of the Superior Court thereof (the same being a Court of Record, having by law a seal), being the officer authorized by the laws of said State of California to make the following certificate, do hereby certify: That Mark E. Levy whose name is subscribed to the Jurat, Affidavit, or Certificate of the Proof or Acknowledgment of the annexed instrument, was, at the time of taking the same, a Notary Public in and for said City and County of San Francisco, residing therein, duly commissioned, qualified and sworn and duly authorized by the laws of said State of California to take Jurats, Affidavits, and the Acknowledgments and Proofs of Deeds or Conveyances for lands, tene-

Exhibit No. 6—(Continued)

ments or hereditaments in said State, to be recorded therein.

I further certify that I am well acquainted with the handwriting of said Notary Public and verily believe that the signature to said Jurat, Affidavit, Acknowledgment or Certificate is genuine, and that the said instrument is executed or acknowledged according to the laws of said State of California. Further that I have compared the impression of the seal affixed thereto with a specimen impression thereof deposited in my office pursuant to law, and that I believe the impression of the seal upon the original certificate is genuine.

In testimony whereof, I have hereunto set my hand and affixed the seal of said Superior Court.

Dated: Sept. 25, 1941.

[Seal] /s/ H. A. VAN DER ZEE,
Clerk.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935.

Territory of Hawaii,
City and County of Honolulu—ss:

W. A. White, being first duly sworn, on oath doth depose and say:

That he is Vice-President of Bishop Trust Com-

Exhibit No. 6—(Continued)

pany, Limited, a Hawaiian corporation, and as such is authorized to make this Affidavit on its behalf;

That said Bishop Trust Company, Limited, is one of the Trustees under the Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor; that said Bishop Trust Company, Limited, a Hawaiian corporation, and Ernest Walter Sultan, as Trustees under Deed of Trust and not in their individual capacity, is a Special Partner in the partnership of Edward D. Sultan Co.; that as Special Partner said Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees as aforesaid, actually have paid into the partnership as a capital contribution the sum of $42,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ W. A. WHITE

Subscribed and sworn to before me this 30th day of September, 1941.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Exhibit No. 6—(Continued)

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935.

Territory of Hawaii,
City and County of Honolulu—ss:

Ernest Walter Sultan, being first duly sworn, on oath doth depose and say:

That he is one of the Trustees under the Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor; that he and Bishop Trust Company, Limited, a Hawaiian corporation, as Trustees under Deed of Trust and not in their individual capacity, are a Special Partner in the partnership of Edward D. Sultan Co.; that as Special Partner they actually have paid into the partnership as a capital contribution the sum of $42,000.00;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ ERNEST WALTER SULTAN

Subscribed and sworn to before me this 13th day of September, 1941.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 7

AMENDMENT TO SPECIAL PARTNERSHIP AGREEMENT

This indenture made this 12th day of January, 1942, by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, Ernest Walter Sultan, of Honolulu aforesaid, Marie Hilda Cohen, of San Francisco, California, and Gabriel Lewis Sultan, of San Francisco aforesaid (hereinafter referred to as "General Partners"), and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor (hereinafter referred to as the "Special Partner"),

Witnesseth That:

Whereas the parties hereto have formed with each other a special partnership by Special Partnership Agreement dated the 30th day of August, 1941; and

Whereas the parties hereto deem it necessary and expedient to alter certain provisions in accordance with the provisions of paragraph 17 (page 14) in said Special Partnership Agreement contained,

Now, therefor, this indenture further witnesseth:

That paragraph 12 (pages 10 and 11) of said Special Partnership Agreement is altered by adding at the end thereof the following:

> "In the event that the aforesaid option is exercised, then Ernest Walter Sultan, if he desires so to act, shall become or continue to act

Exhibit No. 7—(Continued)

as Manager of the business of the partnership, and shall receive as compensation for his services as such a salary, chargeable for purposes of computing net income hereunder as an expenses of the business, in such amount as the General Partners from time to time shall agree upon, constituting the reasonable value of the services rendered to the partnership, but in no event shall his said salary be fixed at less than Three Hundred Fifty Dollars ($350.00) per month. The salary herein provided shall not in any way affect the right of Ernest Walter Sultan so long as he continues to be active in the business of the partnership to receive twenty-five per cent (25%) of the net profits of the partnership as provided in paragraph 4 (pages 4 and 5) of the said Special Partnership Agreement."

and paragraph 18 (page 14) of said Special Partnership Agreement is hereby altered by adding at the end thereof the following:

"Provided, however, that from and after the death of Edward D. Sultan the Special Partnership Agreement shall continue in full force and effect until the end of the fiscal year of the business of the partnership ending in 1953, and that paragraph 12 of said Special Partnership Agreement as herein altered shall not be alterable prior to such date without the consent of all the parties thereto."

In witness whereof the parties hereto have exe-

Exhibit No. 7—(Continued)

cuted these presents as of the day and year first above written.

/s/ EDWARD D. SULTAN,
/s/ ERNEST WALTER SULTAN,
General Partners.
/s/ ERNEST WALTER SULTAN,
BISHOP TRUST COMPANY,
LIMITED,
Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, and not individually, Special Partner.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 12th day of January, 1942, before me personally appeared Edward D. Sultan and Ernest Walter Sultan, to me known to be the persons described in and who executed the foregoing instrument, and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 12th day of January, 1942, before me personally appeared Ernest Walter Sultan, one of the Trustees mentioned in the foregoing instru-

Exhibit No. 7—(Continued)

ment, to me known to be the person described in and who executed the foregoing instrument as Trustee and acknowledged that he executed the same as his free act and deed as such trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

State of California,
City and County of San Francisco—ss:

On this .... day of ....., 194.., before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the foregoing instrument and acknowledged that she executed the same as her free act and deed.

.....
Notary Public in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss:

On this .... day of ....., 194.., before me personally appeared Gabriel Lewis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

.....
Notary Public in and for the City and County of San Francisco, State of California.

EXHIBIT No. 8

AMENDMENT TO SPECIAL PARTNERSHIP AGREEMENT

This indenture made as of this 9th day of June, 1942, by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, Ernest Walter Sultan, of Honolulu aforesaid, Marie Hilda Cohen, of San Francisco, California, and Gabriel Lewis Sultan, of San Francisco aforesaid (hereinafter referred to as "General Partners"), and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor (hereinafter referred to as the "Special Partner"),

Witnesseth that:

Whereas, the parties hereto have formed with each other a special partnership by Special Partnership Agreement dated the 30th day of August, 1941, which said Agreement was amended by Indenture dated the 12th day of January, 1942; and

Whereas, the parties hereto deem it necessary and expedient to alter certain provisions in accordance with the provisions of paragraph 17 (page 14) in said Special Partnership Agreement contained,

Now, therefore, this indenture further witnesseth:

That paragraph 4 (page 4 and 5) of said Special

Exhibit No. 8—(Continued)

Partnership Agreement is hereby amended to read as follows:

"4. Compensation of General Partners and Division of Profits: From time to time and as the General Partners may agree, the General Partners actively engaged in the business of the partnership shall receive as compensation for services rendered to the partnership a salary chargeable, for purposes of computing net profits hereunder, as an expense of the business, in such amount as the General Partners from time to time shall agree upon, constituting the reasonable value of the services rendered to the partnership. All of the remaining net profits of the partnership shall be divided for each annual period in proportion to the above stated interest of each of the partners in the original capital of the partnership, and all losses of the partnership for each annual period shall be divided among the partners in the same manner as herein provided for the division of profits. Any partner may withdraw from the partnership such portion of the profits attributable to the partner's interest as the General Partners may from time to time deem advisable. Amounts not withdrawn shall not be added to the capital account but shall be credited to advance accounts in the names of the respective partners for whom said amounts are being held and interest at the

Exhibit No. 8—(Continued)

rate of five per cent (5%) per annum computed on quarterly balances beginning as of May 1, 1942, and chargeable for the purposes of computing net profits hereunder as an expense of the business, shall be credited to said accounts."

and paragraph 5 (page 5) of said Special Partnership Agreement is hereby amended to read as follows:

"5. Services of the Partners: General Partners, Edward D. Sultan and Ernest Walter Sultan, shall diligently give as much of their time, attention and services to the business of the partnership as they may deem advisable and shall be faithful to the partnership in all transaction relating to said business. Neither of said General Partners shall, without the written consent of all of the partners, employ the capital or credit of the partnership in any other business than that of the partnership, and no partner shall, without the written consent of all of the partners, during the continuation of the partnership carry on or be concerned or interested directly or indirectly in any other business in the Territory of Hawaii which is in direct competition to the business of the partnership."

In witness whereof the parties hereto have ex-

Exhibit No. 8—(Continued)

ecuted these presents as of the day and year first above written.

.....

General Partners.

BISHOP TRUST COMPANY, LIMITED,

By.....

Its Vice President.

By.....

Its

Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, and not individually, Special Partner.

.....

.....—ss:

On this.....day of....., 1943, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

.....

.....

.....—ss:

On this.....day of....., 1943, before me personally appeared Ernest Walter Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowl-

Exhibit No. 8—(Continued)

edged that he executed the same as his free act and deed.

. . . . . .

State of California
City and County of San Francisco—ss:

On this.....day of....., 1943, before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the foregoing instrument and acknowledged that she executed the same as her free act and deed.

. . . . . .

Notary Public in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss:

On this..... day of....., 1943, before me personally appeared Gabriel Lewis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

. . . . . .

Notary Public in and for the City and County of San Francisco, State of California.

. . . . . .

. . . . . —ss:

On this.....day of....., 1943, before me personally appeared Ernest Walter Sultan, Co-

Exhibit No. 8—(Continued)

Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, to me known to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed as such Co-Trustee.

.....

Territory of Hawaii,
City and County of Honolulu—ss:

On this.....day of....., 1943, before me appeared..... and....., to me personally known, who, being by me duly sworn, did say that they are the Vice President and....., respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said ..... and .....acknowledged said instrument to be the free act and deed of said corporation as such Co-Trustee.

.....

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 9

AMENDMENT TO SPECIAL PARTNERSHIP AGREEMENT

This indenture made as of this 2nd day of February, 1945, by and between Edward D. Sultan, of Honolulu, City and County of Honolulu, Territory of Hawaii, Ernest Walter Sultan, of Honolulu aforesaid, Marie Hilda Cohen, of San Francisco, California, and Gabriel Lewis Sultan, of San Francisco aforesaid (hereinafter referred to as "General Partners"), and Ernest Walter Sultan and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, as Settlor (hereinafter referred to as the "Special Partner"),

Witnesseth that:

Whereas, the parties hereto have formed with each other a special partnership by Special Partnership Agreement dated August 30, 1941, which said Agreement was amended by Indentures dated January 12, 1942, and June 9, 1942; and

Whereas, the parties hereto deem it necessary and expedient to alter certain provisions in accordance with the provisions of paragraph 17 (page 14) in said Special Partnership Agreement contained,

Now, therefore, this indenture further witnesseth that:

Exhibit No. 9—(Continued)

Paragraphs 12, 13 and 14 (pages 10, 11 and 12) and Paragraph 18 (page 14) of said Special Partnership Agreement are hereby amended to read as follows:

"12. Termination of Partnership Upon Death of Partner. The death of any general partner shall dissolve the partnership at the end of the current partnership year in which such death shall occur. An audited statement shall be prepared as of that date by the regularly employed independent certified public accountants of the partnership, who shall certify that their examination of the books of accounts and records of the partnership has been made in such detail and in accordance with generally accepted auditing standards applicable in the circumstances, including such tests of accounting records and other supporting evidence and such other procedure as was considered necessary in order to certify that the balance sheet and related statements of income of the partnership fairly presented its position at the end of the period and the results of operation in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

"It shall also be the duty of the independent auditor to certify as to whether or not the outstanding commitments, i.e. obligations of the partnership to buy or sell merchandise for delivery in the future, are likely to disclose a loss, and, if so, the approximate amounts thereof. A reserve shall be provided to take care of such loss, and any losses

Exhibit No. 9—(Continued)

sustained either in obtaining cancellation of said commitments or in their performance shall be charged against said reserve. The determination of the surviving general partners as to whether or not a loss has resulted shall be binding and conclusive upon all the parties and shall be accepted by the personal representatives of the deceased general partner without question or dispute.

"The operations of the partnership may, however, be continued pending the preparation of said audited statement and until thirty days after the receipt by the surviving partners and the estate of the deceased partner of the audited statement herein provided for.

"13. Options on Termination: If general partner, Edward D. Sultan, shall die before the expiration of the partnership, his representative shall have the option (to be declared by notice in writing given to the surviving partners or left at the office of the partnership within said thirty day period (after receipt of the audited statement provided for in paragraph 12), or within a period of six months from the date of death of Edward D. Sultan, whichever is the longer period) of succeeding to or carrying on the interest of the deceased partner in said business as at the end of the partnership year in which such death shall occur, either as a general partner, in accordance with law, as a special partner, or as a limited partner under the provisions of Act 162, Session Laws of Hawaii 1943, as the same now are or as the same may from time

Exhibit No. 9—(Continued)

to time be amended; and notwithstanding any of the provisions of the preceding paragraph of this agreement to the contrary, the operations of the partnership shall be continued during the period in which the option may be exercised. If such option shall be exercised, the surviving partners agree that they will enter into a partnership agreement with the representative of said deceased partner so that the said business shall be carried on during the residue of said term as from the end of the partnership year in which the death of said Edward D. Sultan shall occur as nearly as may be according to the provisions of these presents, but so that the representative of said Edward D. Sultan shall succeed to his share in said business and be substituted for him as a dormant general partner, as a special partner or as a limited partner; provided that in the case the representative of said Edward D. Sultan shall elect to become a dormant general partner, a special partner or a limited partner by virtue of such option as aforesaid, all proper instruments for carrying out the provisions of this present clause shall be executed and made between the representative and the surviving partners, and all proper notices, publications, petitions or court proceedings shall be made and executed or taken at the expense of the partnership.

"In the event of the death of any general partner, other than Edward D. Sultan, an option during the said period of thirty days (after the receipt of the audited statement provided for in paragraph

Exhibit No. 9—(Continued)

12), is hereby granted to said Edward D. Sultan to purchase the interest in the partnership of such deceased general partner (said option to be exercised by notice in writing given to the executor or administrator, if any, or, if none, then left at the office of the partnership) for an amount equivalent to the fair value thereof as determined by the auditor's statement, or by the value of the interest as shown on the books of account of the partnership, whichever amount is less. In determining the fair value of such interest, no value shall be attributable to good will. Edward D. Sultan shall have a like option to purchase the interest of any general partner who may give notice to terminate the partnership by giving notice in writing to such partner and leaving a copy of the notice at the office of the partnership within three (3) months of the notice to terminate.

"If Edward D. Sultan shall exercise his option and the purchase is consummated, the same shall be considered as effective at the end of the partnership year in which such death occurred or the notice of intention to terminate the partnership was given, and the partner desiring to terminate the partnership or the estate of such deceased partner, as the case may be, shall not be entitled to receive any share of the net profits from and after said date, but shall be entitled to receive interest at the current bank rate upon the amount to be paid for the deceased partner's interest from said date. Said Edward D. Sultan shall have the right

Exhibit No. 9—(Continued)

to make payments therefor at such time or times not later than five (5) years after the date when the said option to purchase the deceased partner's interest was exercised as he may deem advisable.

"14. Winding up on Death of General Partner: In case the representative of said Edward D. Sultan shall not exercise his option to succeed to the deceased partner's share in said business as a general, special or limited partner, and in the event of the death of any other general partner except said Edward D. Sultan, the said Edward D. Sultan shall not purchase the interest of said deceased general partner, said partnership shall be placed in liquidation. Thereupon the debts of the partnership shall be first paid as satisfactorily provided for before any distribution shall be made to the general partners or the estate of the deceased partner.

"18. Term of Partnership: The term of the partnership shall be for a period commencing with the date of execution hereof and ending January 31, 1946, and, subject to the provisions of paragraph 11 hereinabove, shall continue from year to year ending January 31st of each year thereafter until terminated at the end of the partnership year in which any general partner shall give written notice of his or her intention to terminate the partnership by leaving the same at the office of the partnership not less than three (3) months prior to the end of said partnership year."

In witness whereof the parties hereto have ex-

Exhibit No. 9—(Continued)

ecuted these presents as of the day and year first above written.

/s/ EDWARD D. SULTAN,
/s/ ERNEST WALTER SULTAN,
/s/ MARIE HILDA COHEN,
/s/ GABRIEL LEWIS SULTAN,
General Partners.

/s/ ERNEST WALTER SULTAN,
[Seal] BISHOP TRUST COMPANY,
LIMITED,
By /s/ W. A. WHITE,
Its Vice-President.
By /s/ E. BENNER, JR.,
Its Vice-President.
Trustees under Deed of Trust of Edward D. Sultan dated August 28, 1941, and not individually, Special Partner.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 2nd day of February, 1945, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Exhibit No. 9—(Continued)

State of New York,
County of New York—ss:

On this 26th day of February, 1945, before me personally appeared Ernest Walter Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MORTIMER LANDSBERG,
Mortimer Landsberg, Notary Public Queens Co. Clk. No. 3445, Reg. No. 205-L-5 N. Y. Co. Clk. No. 845, Reg. No. 497-L-5.

State of California,
City and County of San Francisco—ss:

On this 10th day of February, 1945, before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the foregoing instrument and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ THOMAS J. O'CONNOR,
Notary Public in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss:

I, H. A. van der Zee, County Clerk of the City and County of San Francisco, State of California, and ex-officio Clerk of the Superior Court thereof (the same being a Court of Record, having by law

Exhibit No. 9—(Continued)

a seal), being the officer authorized by the laws of said State of California to make the following certificate, do hereby certify: That Thomas J. O'Connor, whose name is subscribed to the Jurat, Affidavit, or Certificate of the Proof or Acknowledgment of the annexed instrument, was, at the time of taking the same, a Notary Public in and for said City and County of San Francisco, residing therein, duly commissioned, qualified and sworn and duly authorized by the laws of said State of California to take Jurats, Affidavits, and the Acknowledgments and Proofs of Deeds or Conveyances for lands, tenements or hereditaments in said State, to be recorded therein.

I further certify that I am well acquainted with the handwriting of said Notary Public and verily believe that the signature to said Jurat, Affidavit, Acknowledgment or Certificate is genuine, and that the said instrument is executed or acknowledged according to the laws of said State of California. Further that I have compared the impression of the seal affixed thereto with a specimen impression thereof deposited in my office pursuant to law, and that I believe the impression of the seal upon the original certificate is genuine.

In testimony whereof, I have hereunto set my hand and affixed the seal of said Superior Court.

Dated: Feb. 10, 1945.

[Seal] /s/ H. A. VAN DER ZEE, Clerk.

Exhibit No. 9—(Continued)

State of California,
City and County of San Francisco—ss:

On this 9th day of February, 1945, before me personally appeared Gabriel Lewis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ THOMAS J. O'CONNOR,
Notary Public in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss:

I, H. A. van der Zee, County Clerk of the City and County of San Francisco, State of California, and ex-officio Clerk of the Superior Court thereof (the same being a Court of Record, having by law a seal), being the officer authorized by the laws of said State of California to make the following certificate, do hereby certify: That Thomas J. O'Connor, whose name is subscribed to the Jurat, Affidavit, or Certificate of the Proof or Acknowledgment of the annexed instrument, was, at the time of taking the same, a Notary Public in and for said City and County of San Francisco, residing therein, duly commissioned, qualified and sworn and duly authorized by the laws of said State of California to take Jurats, Affidavits, and the Acknowledgments and Proofs of Deeds or Conveyances for lands, tene-

Exhibit No. 9—(Continued)

ments or hereditaments in said State, to be recorded therein.

I further certify that I am well acquainted with the handwriting of said Notary Public and verily believe that the signature to said Jurat, Affidavit, Acknowledgment or Certificate is genuine, and that the said instrument is executed or acknowledged according to the laws of said State of California. Further that I have compared the impression of the seal affixed thereto with a specimen impression thereof deposited in my office pursuant to law, and that I believe the impression of the seal upon the original certificate is genuine.

In testimony whereof, I have hereunto set my hand and affixed the seal of said Superior Court.

Dated: Feb. 9, 1945.

[Seal] /s/ H. A. VAN DER ZEE, Clerk.

State of New York,
County of New York—ss:

On this 26th day of February, 1945, before me personally appeared Ernest Walter Sultan, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, to me known to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed as such Co-Trustee.

[Seal] /s/ MORTIMER LANDSBERG,
Notary Public Queens Co. My Commission expires March 30, 1945.

Exhibit No. 9—(Continued)

State of New York,
County of New York—ss:

I, Archibald R. Watson, County Clerk and Clerk of the Supreme Court, New York County, the same being a Court of Record having by law a seal, do hereby certify, that Mortimer Landsberg whose name is subscribed to the annexed deposition, certificate of acknowledgment or proof, was at the time of taking the same a Notary Public acting in and for said County, duly commissioned and sworn, and qualified to act as such; that he has filed in the Clerk's office of the County of New York a certified copy of his appointment and qualification as a Notary Public for the County of Queens with his autograph signature; that as such Notary Public he was duly authorized by the laws of the State of New York to protect notes, to take and certify depositions, to administer oaths and affirmations, to take affidavits and certify the acknowledgment or proof of deeds and other written instruments for lands, tenements and hereditaments, to be read in evidence or recorded in this State. And further, that I am well acquainted with the handwriting of such Notary Public, or have compared the signature of such officer with his autograph signature filed in my office, and believe that the signature to the said annexed instrument is genuine.

In witness whereof, I have hereunto set my hand

Exhibit No. 9—(Continued)

and affixed my official seal this 27th day of February, 1945.

[Seal] /s/ ARCHIBALD R. WATSON,
County Clerk and Clerk of the Supreme Court, New York County.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 16th day of April, 1945, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice-President and Vice-President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and E. Benner, Jr. acknowledged said instrument to be the free act and deed of said corporation as such Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 10

This indenture made this.....day of..... A.D. 1949, by and among Edward D. Sultan, of the City and County of Honolulu, Territory of Hawaii, Ernest Walter Sultan, formerly of Honolulu and presently residing in Los Angeles, California, Marie Hilda Cohen, of San Francisco, California, and Gabriel Lewis Sultan, of San Francisco, California, (hereinafter referred to as "General Partners", and Ernest Walter Sultan and Bishop Trust Company, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan, Settlor, (hereinafter referred to as "Special Partners"),

Witnesseth that:

Edward D. Sultan, Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan are presently General Partners, and Ernest Walter Sultan and Bishop Trust Company, Trustees as aforesaid, are presently Special Partners under a Special Partnership Agreement dated August 30, 1941, as amended by Agreements dated January 12, 1942, June 9, 1942, and February 2, 1945.

The parties hereto deem it necessary and expedient to further amend said agreement and to alter certain provisions thereof as provided for in paragraph 17 of the main agreement (page 14).

Now, therefore, this Indenture witnesseth that:

At the close of business on January 31, 1949, Ernest Walter Sultan (formerly of Honolulu and

Exhibit No. 10—(Continued)

presently residing in Los Angeles, California), Marie Hilda Cohen (of San Francisco, California) and Gabriel Lewis Sultan (of San Francisco, California), withdraw as General Partners in said partnership, and shall from and after January 31, 1949, cease to have any interest in the said partnership or the profits or losses thereof, and they shall have returned to them their capital contributions together with any accrued and unwithdrawn profits to January 31, 1949, within ten (10) days after the determination of such profits by the regularly employed independent public accountants of the partnership.

The withdrawing partners further agree to execute any and all instruments, receipts, acquittances and releases that may be required to effect their withdrawal from said partnership, and each of said General Partners does hereby nominate, constitute and appoint Edward D. Sultan, of the City and County of Honolulu, Territory of Hawaii, as their respective true and lawful attorney-in-fact for each of them, and in each of their names and as such attorney-in-fact to execute and deliver any and all instruments required in law to effect their withdrawal from said partnership, and to terminate their interests therein, with full power and authority to receipt for all sums of money due to them, and to give acquittances and releases therefor, as fully and effectually as each one of them could do personally, hereby ratifying, approving and confirming any action taken by their said attorney-

Exhibit No. 10—(Continued)

in-fact or by any person whom he may lawfully substitute to act as attorney-in-fact.

This agreement shall extend to and bind all of the parties hereto, their respective heirs, executors, administrators, successors and assigns.

In witness whereof, the parties hereto have executed these presents as of the day and year first above written.

Signed, Sealed and Delivered in the presence of:

[Seal] .....
Edward D. Sultan
[Seal] /s/ ERNEST WALTER SULTAN,
[Seal] /s/ MARIE HILDA COHEN,
[Seal] /s/ GABRIEL LEWIS SULTAN,
General Partners.
[Seal] /s/ ERNEST WALTER SULTAN,
BISHOP TRUST COMPANY,
By.....
Trustees under Deed of Trust dated August 28, 1941, of Edward D. Sultan, Settlor, Special Partners.

State of California,
County of Los Angeles—ss:

On this 28th day of January, A.D. 1949, before me, Harriett R. Barker, a Notary Public in and for said County and State, personally appeared Ernest Walter Sultan, known to me to be the person whose name is subscribed to the within instru-

Exhibit No. 10—(Continued)

ment, and acknowledged to me that he executed the same.

In witness whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Seal] /s/ HARRIETT R. BARKER,
Notary Public in and for said County and State.
My Commission expires January 26, 1950.

(Acknowledgment—General—Wolcotts Form 233)

State of California, (Foreign)
County of Los Angeles—ss:

I, W. G. Sharp, County Clerk and Clerk of the Superior Court of the State of California, in and for the County of Los Angeles, which Court is a Court of Record, having by law a seal do hereby certify that Harriett R. Barker whose name is subscribed to the attached certificate of acknowledgment, proof or affidavit, was at the time of taking said acknowledgment, proof or affidavit, a Notary Public in and for Los Angeles County, duly commissioned and sworn and residing in said County, and was, as such, an officer of said State, duly authorized by the laws thereof to take and certify the same, as well as to take and certify the proof and acknowledgment of deeds and other instruments in writing to be recorded in said State, and that full faith and credit are and ought to be given to his official acts; that the certificate of such officer

Exhibit No. 10—(Continued)

is required to be under seal; that the impression of his official seal is not required by law to be on file in the office of the County Clerk; I further certify that I am well acquainted with his handwriting, and verily believe that the signature to the attached certificate is his genuine signature, and further that the annexed instrument is executed and acknowledged according to the laws of the State of California.

In witness whereof, I have hereunto set my hand and annexed the seal of the Superior Court of the State of California, in and for the County of Los Angeles, this 29th day of January, 1949.

[Seal] /s/ W. G. SHARP,
County Clerk and Clerk of the Superior Court of the State of California, in and for the County of Los Angeles.

State of California,
City and County of San Francisco—ss:

On this 26th day of January, A.D. 1949, before me, Alice E. Lowrie, a Notary Public in and for the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Marie Hilda Cohen and Gabriel Lewis Sultan, known to me to be the persons whose names are subscribed to the within instrument, and acknowledged to me that they executed the same.

In witness whereof, I have hereunto set my hand

Exhibit No. 10—(Continued)

and affixed my official seal the day and year in this Certificate first above written.

[Seal] /s/ ALICE E. LOWRIE,
Notary Public, in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss:

I, Martin Mongan, County Clerk and Clerk of the Superior Court of the State of California, in and for the City and County of San Francisco, which Court is a Court of Record, having by law a seal, do hereby certify: That Alice E. Lowrie, whose name is subscribed to the attached certificate of acknowledgment, proof or affidavit, was at the time of taking said acknowledgment, proof or affidavit, a Notary Public in and for the City and County of San Francisco, duly commissioned and sworn and residing in said City and County, and was, as such, an officer of said State, duly authorized by the laws thereof to take and certify the same, as well as to take and certify the proof and acknowledgment of deeds and other instruments in writing to be recorded in said State, and that full faith and credit are and ought to be given to his official acts; that the certificate of such officer is required to be under seal; that the impression of his official seal is not required by law to be on file in the office of the County Clerk; I further certify that I am well acquainted with his handwrit-

Exhibit No. 10—(Continued)

ing and verily believe that the signature to the attached certificate is his genuine signature, and further that the annexed instrument is executed and acknowledged according to the laws of the State of California.

In witness whereof, I have hereunto set my hand and annexed the seal of the Superior Court of the State of California, in and for the City and County of San Francisco.

Dated: January 27, 1949.

[Seal] /s/ MARTIN MONGAN, Clerk.

State of California,
City and County of San Francisco—ss:

Marie Hilda Cohen and Gabriel Lewis Sultan, being first duly sworn, each for herself and himself, deposes and says:

That he has executed the foregoing amendment to agreement for limited partnership; that he has read the foregoing agreement and knows the contents thereof and that the same is true of his own knowledge.

/s/ MARIE HILDA COHEN
/s/ GABRIEL LEWIS SULTAN

Subscribed and sworn to before me, this 26th day of January, 1949.

[Seal] /s/ ALICE E. LOWRIE,
Notary Public, in and for the City and County of San Francisco, State of California.

Exhibit No. 10—(Continued)

State of California,
County of Los Angeles—ss:

Ernest Walter Sultan, being first duly sworn, deposes and says:

That he has executed the foregoing amendment to agreement for limited partnership; that he has read the foregoing agreement and knows the contents thereof, and that the same is true of his own knowledge.

/s/ ERNEST WALTER SULTAN

Subscribed and sworn to before me this 28th day of January, 1949.

[Seal] /s/ HARRIETT R. BARKER,
Notary Public, in and for the County of Los Angeles, State of California.

State of California,
County of Los Angeles—ss:

Ernest Walter Sultan, being first duly sworn, deposes and says:

That he has executed the foregoing amendment to agreement for limited partnership as one of the trustees under deed of trust dated August 28, 1941, of Edward D. Sultan, Settlor; that he has read the foregoing agreement and knows the contents thereof, and that the same is true of his own knowledge.

/s/ ERNEST WALTER SULTAN

Exhibit No. 10—(Continued)

Subscribed and sworn to before me this 28th day of January, 1949.

[Seal] /s/ HARRIETT R. BARKER,
Notary Public, in and for the County of Los Angeles, State of California.

EXHIBIT NO. 11

[Letterhead of Edward D. Sultan Co.]

Ernest Walter Sultan and Feb. 1, 1949
Bishop Trust Company, Limited, Trustees
C/o Bishop Trust Company, Limited,
Honolulu, T. H.

Gentlemen:

Now that my son, Edward Dexter Sultan, Jr., has reached his majority, and having worked for the company during the last several summers, and being about to graduate from college so that he will be able to devote his full time to the business, he as well as I am desirous of arranging to have him acquire an interest in the Edward D. Sultan Co.

As you know, the main reason for setting up the Trust was to try to interest him in the business so that he could, in due course, take it over.

At the present time, due to changes in business conditions that necessitate larger investments in stock and, also because of the slowing down of the receipt of payments on accounts receivable, I believe that the capital of the company will have to be increased to not less than $250,000.00.

Exhibit No. 11—(Continued)

In order to get new money into the business, through sale of an interest therein to my wife, as well as to serve the purpose of getting my son into the business, I would like to purchase your interest in Edward D. Sultan Co. on behalf of my son and wife. I have arranged to purchase, from Ernest Walter Sultan, Marie Hilda Cohen and Gabriel Lewis Sultan, their interests in the partnership, and it is my proposal that my son shall purchase a 25% interest and my wife a 24% interest, leaving me a 51% interest in the business.

To accomplish this purpose, I offer to purchase from you your 42% interest in Edward D. Sultan Co. for cash, payable as follows: A sum equivalent to your capital investment plus your unpaid profits held by the partnership accumulated to January 31, 1948, immediately upon acceptance of this offer; the balance due you, representing earnings for the year ended January 31, 1949, will be paid to you immediately upon receipt of our auditor's statement showing the balance due you. As settlor of the Trust, I will consent to such sale, and my son, Edward Dexter Sultan, Jr., will also consent as the beneficiary.

Your prompt consideration of this proposal will be appreciated.

Very truly yours,

/s/ EDWARD D. SULTAN.

EDS:ne

EXHIBIT No. 12

[Letterhead of Bishop Trust Company, Limited]

Mr. Edward D. Sultan February 9, 1949
Edward D. Sultan Co.
P.O. Box 301, Honolulu 9, Hawaii

Re: Edward D. Sultan Trust

Dear Mr. Sultan:

Acknowledgment is made of your letter addressed to Ernest Walter Sultan and Bishop Trust Company, Ltd., Trustees of the Edward D. Sultan Trust, offering to purchase from the Trust its 42% interest in the Edward D. Sultan Co. Your offer as outlined in the fifth paragraph of your letter is acceptable to us co-Trustee, provided we are furnished with a consent and approval of the sale by Ernest Walter Sultan, our co-Trustee, and formal approval and consent by yourself as Settlor and your son, Edward D. Sultan, Jr., as beneficiary. These latter two consents could be prepared in a formal way by Mr. Milton Cades in a manner that would be suitable for the Trust records. A simple letter by the co-Trustee approving of the sale as outlines in your letter would be sufficient from him.

We would call to your attention the fact that inasmuch as payments of $300 per month are to be made from the income of the Trust from now on to your son until he attains the age of thirty years, major changes in the portfolio of the Trust will be necessitated in order to have securities therein that will produce sufficient income each year to insure

Exhibit No. 12—(Continued)

these monthly payments. When the sale of the business goes through, we will make a review of the portfolio and will make recommendations to our co-Trustee and yourself.

Very truly yours

/s/ E. BENNER, Jr.
Vice-President.

EB:GED

EXHIBIT No. 13

BILL OF SALE

This indenture, made as of the close of business on January 31, 1949, by and between Edward D. Sultan Co., a special partnership composed of Edward D. Sultan of Honolulu, City and County of Honolulu, Territory of Hawaii, as General Partner, and Ernest Walter Sultan of Los Angeles, County of Los Angeles, State of California, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated August 28, 1941, made by Edward D. Sultan as Settlor, as Special Partner, hereinafter called the "Seller", and Edward D. Sultan, Olga L Sultan and Edward D. Sultan, Jr., copartners doing business under the firm name and style of Edward D. Sultan Co., hereinafter called the "Purchaser",

Witnesseth That:

The Seller, for and in consideration of the sum of One Dollar ($1.00), lawful money of the United States of America, and other good and valuable

Exhibit No. 13—(Continued)

consideration to it paid, the receipt whereof is hereby acknowledged, does hereby grant, bargain, sell, assign, transfer, set over, confirm and deliver unto the Purchaser, and its successors and assigns, forever:

All and singular, the rights, property, assets and privileges owned by the Seller, as shown on the statement of assets and liabilities prepared by Tennent & Greany, dated as of the close of business on January 31, 1949, a copy of which is attached hereto, incorporated herein and made a part hereof for all purposes, including particularly, but not in anywise limiting the generality of the foregoing, all chattels, leaseholds, improvements, machines and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, books, accounts, inventories, together with all other personal property, goods and chattels of every kind and description and wheresoever situate, all good will, trade names, trade connections, licenses and all contracts and agreements, including any and all rights under policies of indemnity, fidelity or other bonds or insurance of any and every kind, or cash on hand or in bank or banks, bonds, mortgages, conditional sales agreements, accounts and bills receivable, promissory notes, claims, demands, equities and choses in action, and all other property and assets, tangible and intangible, of every kind or nature, owned or claimed by the Seller and shown on said balance sheet.

Exhibit No. 13—(Continued)

To Have and to Hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits and appurtenances to the same or any part thereof belonging or appertaining, or held and enjoyed therewith, unto the Purchaser, its successors and assigns, absolutely and forever, or in fee simple, as the case may be.

And the Purchaser, in consideration of the foregoing, does hereby covenant and agree that it will, and by these presents does assume all of the liabilities, obligations and indebtedness of the Seller shown on said statement of assets and liabilities attached hereto, and does covenant and agree to pay and discharge the same as fully and completely as though the said liabilities, obligations and indebtedness had been incurred directly by said Purchaser, and to indemnify and hold harmless the said Seller from all liability, expense or obligations upon the same or arising in connection therewith.

And for the consideration aforesaid, the Seller, for itself, its successors and assigns, does hereby irrevocably appoint the Purchaser, its successors and assigns, its true and lawful attorney, in its name, place and stead, to ask, demand, sue for and recover any and all moneys, assets, or other property conveyed and transferred hereby or intended so to be, and the rights and benefits thereof, and does further covenant that it, the Seller, will at any time at the request of the partnership make, do, execute and deliver all such receipts, powers of

Exhibit No. 13—(Continued)

attorney and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property, claims and demands hereinabove conveyed and assigned, or intended so to be, as the Purchaser reasonably may require.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

EDWARD D. SULTAN CO.,
a special partnership
/s/ EDWARD D. SULTAN,
General Partner

/s/ ERNEST WALTER SULTAN,
[Seal] BISHOP TRUST COMPANY,
LIMITED
By /s/ E. BENNER, JR.,
Its Vice President
By /s/ W. E. HARRISON,
Its Vice President
Trustees as aforesaid
Special Partner, Seller

EDWARD D. SULTAN CO.,
a co-partnership

/s/ EDWARD D. SULTAN,
/s/ OLGA L. SULTAN,
/s/ EDWARD D. SULTAN, JR.
Purchaser

Exhibit No. 13—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 21st day of February, 1949, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

State of California,
County of Los Angeles—ss.

On this 24th day of Feb., 1949, before me personally appeared Ernest Walter Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed in his individual capacity and as Co-Trustee under deed of trust of Edward D. Sultan.

[Seal] /s/ HARRIETT R. BARKER,
Notary Public, Los Angeles County, California. My Commission expires January 26, 1950.

State of California,
County of Los Angeles—ss.

I, W. G. Sharp, County Clerk and Clerk of the Superior Court of the State of California, in and

Exhibit No. 13—(Continued)

for the County of Los Angeles, which Court is a Court of Record, having by law a seal do hereby certify that Harriett R. Barker whose name is subscribed to the attached certificate of acknowledgment, proof or affidavit, a Notary Public in and for Los Angeles County, duly commissioned and sworn and residing in said County, and was, as such, an officer of said State, duly authorized by the laws thereof to take and certify the same, as well as to take and certify the proof and acknowledgments of deeds and other instruments in writing to be recorded in said State, and that full faith and credit are and ought to be given to his official acts; that the certificate of such officer is required to be under seal; that the impression of his official seal is not required by law to be on file in the office of the County Clerk; I further certify that I am well acquainted with his handwriting, and verily believe that the signature to the attached certificate is his genuine signature, and further that the annexed instrument is executed and acknowledged according to the laws of the State of California.

In Witness Whereof, I have hereunto set my hand and annexed the seal of the Superior Court of the State of California, in and for the County of Los Angeles, this 25th day of Feb., 1949.

[Seal] /s/ W. G. SHARP,

County Clerk and Clerk of the Superior Court of the State of California, in and for the County of Los Angeles.

Exhibit No. 13—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 8th day of March, 1949, before me appeared E. Benner, Jr. and W. E. Harrison, to me personally known, who, being by me duly sworn, did say that they are the Vice President and Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr. and W. E. Harrison acknowledged said instrument to be the free act and deed of said corporation as such Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of March, 1949, before me personally appeared Olga L. Sultan, to me known to be the person described in and who executed the

Exhibit No. 13—(Continued)

foregoing instrument, and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

State of California,
County of San Mateo—ss.

On this 1st day of March, 1949, before me personally appeared Edward D. Sultan, Jr., to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MABEL WEAVER,
Notary Public in and for the County of San Mateo, State of California. My Commission expires Oct. 17, 1952.

State of California,
County of San Mateo—ss.

I, W. H. Augustus, County Clerk of the County of San Mateo, State of California, and ex-officio clerk of the Superior Court thereof, the same being a Court of Records, having by law, a seal, do hereby certify, That Mabel Weaver whose name is subscribed to the Certificate of the proof or acknowledgment of the annexed instrument and thereon written, was at the time of taking of such proof and acknowledgment, a Notary Public, in and for said County, residing therein, duly commissioned

Exhibit No. 13—(Continued)

and sworn, and duly authorized by the laws of said State to administer oaths, take acknowledgments and proofs of deeds or conveyances, for land, tenements or hereditaments in said State, to be recorded therein. And further that I am well acquainted with the handwriting of such Notary Public, and verily believe that the signature of said Certificate of proof or acknowledgment is genuine, and that said instrument is executed and acknowledged according to the laws of said State. I further certify that an impression of the seals of Notaries Public is not required by law to be filed in my office.

In Testimony Whereof, I have hereunto set my hand and affixed the seal of the said Superior Court, this 1st day of March, 1949.

[Seal] W. H. AUGUSTUS, County Clerk
By /s/ GERTRUDE V. HOVIG, Deputy

Edward D. Sultan Company
Statement of Financial Position
January 31, 1949

Current Assets		
Cash on Hand and in Banks		$151,764.83
Accounts Receivable—Less Estimated Uncollectible	$13,036.51	98,459.04
Merchandise Inventory—Lower of Cost or Market		94,270.38
Prepaid Rent, Deposits, Etc.		1,300.00
Total Current Assets		$345,794.25

Exhibit No. 13—(Continued)

Other Assets		
Leasehold Improvements and Equipment—Less Accrued Depreciation	$16,584.14	42,758.33
Total Assets		$388,552.58
Less Current Liabilities		
Accounts Payable, Accrued Bonus and Sundry Taxes		$ 30,551.89
Capital and Credit Balances Payable to Partners of Terminated Partnership:		
Trustees for Edward D. Sultan, Jr.		137,357.62
Edward D. Sultan		66,072.81
Ernest W. Sultan		9,023.42
Gabriel L. Sultan		9,023.42
Marie H. Cohen		9,023.42
Total Current Liabilities		$261,052.58
Edward D. Sultan—Capital and Credit Balance		$127,500.00

EXHIBIT No. 14

STATEMENT OF DISSOLUTION OF THE SPECIAL PARTNERSHIP

Of Edward D. Sultan Co., Honolulu, County of Honolulu, T. H., February 21, 1949.

To the Treasurer of the Territory of Hawaii, Honolulu, T. H.

Sir:—

This Is to Certify, That on the first day of

Exhibit No. 14—(Continued)

February, 1949, the Special Partnership firm of Edward D. Sultan Co., maintaining and carrying on a wholesale and retail jewelry business at Honolulu in the district of Honolulu, County of Honolulu, Territory of Hawaii, was dissolved by mutual consent, and in compliance with law, the following statement is herewith filed.

That the Partners of the said Special Partnership firm at the date of the dissolution were:

Edward D. Sultan, residing at Honolulu, T. H.; Ernest Walter Sultan, residing at Los Angeles, California; Marie Hilda Cohen, residing at San Francisco, California; Gabriel Louis Sultan, residing at San Francisco, California; General Partners.

Ernest Walter Sultan and Bishop Trust Company, Limited, Trustees under Deed of Trust of Edward D. Sultan, Los Angeles, California; Honolulu, T.H., Special Partner.

[Stamped]: Paid Mar. 11, 1949, Treasurer's Office, Territory of Hawaii.

Witness our hands this 21st day of February, A.D., 1949.

/s/ EDWARD D. SULTAN,
/s/ ERNEST W. SULTAN,
/s/ MARIE HILDA COHEN,
/s/ GABRIEL LOUIS SULTAN,
/s/ ERNEST WALTER SULTAN,
[Seal] BISHOP TRUST COMPANY, LIMITED
/s/ By E. BENNER, JR., Its Vice Pres.
/s/ By W. E. HARRISON, Its Vice Pres.

Exhibit No. 14—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 21st day of February, 1949, before me personally appeared Edward D. Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.
[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6/30/49.

State of California,
County of Los Angeles—ss.

On this 24th day of Feb., 1949, before me personally appeared Ernest Walter Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed in his individual capacity and as Co-Trustee under deed of trust of Edward D. Sultan.

[Seal] /s/ HARRIET R. BARKER,
Notary Public, Los Angeles County, Calif. My Commission Expires January 26, 1950.

State of California,
County of Los Angeles—ss.

On this 24th day of Feb., 1949, before me personally appeared Marie Hilda Cohen, to me known to be the person described in and who executed the

Exhibit No. 14—(Continued)

foregoing instrument, and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ HARRIET R. BARKER,
Notary Public, Los Angeles County, Calif. My Commission expires January 26, 1950.

State of California,
County of Los Angeles—ss.

On this 24th day of Feb., 1949, before me personally appeared Gabriel Louis Sultan, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ HARRIET R. BARKER,
Notary Public, Los Angeles County, Calif. My Commission Expires January 26, 1950.

State of California,
County of Los Angeles—ss. (Foreign)

I, W. G. Sharp, County Clerk of the Superior Court of the State of California, in and for the County of Los Angeles, which Court is a Court of Record, having by law a seal do hereby certify that Harriet R. Barker whose name is subscribed to the attached certificate of acknowledgment, proof or affidavit, was at the time of taking said acknowledgment, proof or affidavit, a Notary Public in and for Los Angeles County, duly commissioned and sworn and residing in said County, and was, as such, an officer of said State, duly authorized by the laws

Exhibit No. 14—(Continued)

thereof to take and certify the same, as well as to take and certify the proof and acknowledgment of deeds and other instruments in writing to be recorded in said State, and that full faith and credit are and ought to be given to his official acts; that the certificate of such officer is required to be under seal; that the impression of his official seal is not required by law to be on file in the office of the County Clerk; I further certify that I am well acquainted with his handwriting, and verily believe that the signature to the attached certificate is his genuine signature, and further that the annexed instrument is executed and acknowledged according to the laws of the State of California.

In Witness Whereof, I have hereunto set my hand and annexed the seal of the Superior Court of the State of California, in and for the County of Los Angeles, this 25th day of Feb., 1949.

[Seal] /s/ W. G. SHARP,
County Clerk and Clerk of the Superior Court of the State of California, in and for the County of Los Angeles.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 8th day of March, 1949, before me appeared E. Benner, Jr. and W. E. Harrison, to me personally known, who, being by me duly sworn, did say that they are the Vice President and Vice President, respectively, of Bishop Trust Company,

Exhibit No. 14—(Continued)

Limited, a Hawaiian corporation, Co-Trustee under Deed of Trust of Edward D. Sultan dated August 28, 1941, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr. and W. E. Harrison acknowledged said instrument to be the free act and deed of said corporation as such Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

EDWARD D. SULTAN TRUST

Schedule of Income and Expense
August 28, 1941 to August 28, 1950 Inclusive

	Fiscal Year Ending August 28									
	1942	1943	1944	1945	1946	1947	1948	1949	1950	Total
Income										
Distributive share of profits and (losses) of Edward D. Sultan Co. for fiscal year ending January 31	$24,754.29	$114,112.68	$154,097.03	$200,029.40	$ 99,698.24	$ 40,341.86	$46,425.64	$ 10,745.87		
Dividends received on stocks	65.62	1,803.14	3,186.27						$ 1,882.14	
Interest received on notes receivable								300.00		
Net gains or (losses) on sale of securities			5,250.33					(340.56)		
Interest received on U. S. Treasury Certificates									525.00	
	24,819.91	115,915.72	162,533.63	200,029.40	99,698.24	40,341.86	46,425.64	10,705.31	2,407.14	$702,876.85
Expense										
Trustee fees	300.82	1,259.30	1,772.27	2,100.29	1,046.98	453.42	514.26	172.46	120.36	
Tax service fees		10.00	35.00	50.00	50.00	50.00	50.00	100.00	100.00	
Federal income taxes		4,932.17	44,932.30	100,547.42	139,750.04	109,492.83	48,254.64	21,139.35	9,241.55	
Territorial income taxes		335.74	2,218.82	3,146.04	2,548.78	1,285.82		190.44	63.50	
Territorial C. and D. on Mainland dividends		4.68	82.40							
Bank charges, postage and miscellaneous		.45	11.85		11.64			.05	.55	
War damage insurance on securities		1.65	1.65							
	300.82	6,543.99	49,054.29	105,843.75	143,407.44	111,282.07	48,818.90	21,602.30	9,525.96	496,379.52
Net Income	$24,519.09	$109,371.73	$113,479.34	$ 94,185.65	$(43,709.20)	$(70,940.21)	$(2,393.26)	$(10,896.99)	$(7,118.82)	$206,497.33
Less: Income distributed								$ 2,400.00	$ 3,600.00	6,000.00
										$200,497.33
Add: Gift by Edward D. Sultan										42,000.00
Trust Balance - Inventory Attached										$242,497.33

EDWARD D. SULTAN TRUST

Schedule of Receipts of Distributive Share of Income
of Edward D. Sultan Co.

Exhibit 24

	Fiscal Year Ending January 31								
	1942	1943	1944	1945	1946	1947	1948	1949	Total
Distributive share of income	$24,754.29	$114,113.58	$154,097.03	$200,029.40	$99,698.24	$40,341.86	$46,425.64	$10,745.87	$690,204.91
Payments made:									
June 23, 1942	24,754.29								
March 15, 1943		3,000.00							
March 23, 1943		108,913.64							
October 8, 1943		2,198.94							
March 15, 1944			15,640.00						
June 14, 1944			19,000.00						
September 2, 1944			21,000.00						
September 21, 1944			97,457.03						
March 12, 1945				83,029.40					
March 17, 1945				50,000.00					
March 21, 1945				25,000.00					
April 6, 1946				42,000.00					
May 21, 1946					99,698.24				
January 14, 1949						2,155.75			
March 14, 1949						10,000.00			
April 28, 1949						28,186.11	46,425.64	10,745.87	
	$24,754.29	$114,113.58	$154,097.03	$200,029.40	$99,698.24	$40,341.86	$46,425.64	$10,745.87	$690,204.91

EDWARD D. SULTAN TRUST

Inventory of Assets
August 28, 1950

Cash			$ 9,842.58
Bonds			
U. S. Savings Bonds			
$ 6,500.00 maturity value - Series "F" due July 1,1954	$4,810.00		
34,000.00 " " " " " March 1,1955	25,160.00		
135,000.00 " " " " " May 1, 1956	99,900.00	$129,870.00	
U. S. Treasury Bonds - Series "A" - 1-1/8% due Jan. 1, 1951		42,002.61	171,872.61
Note Receivable			
Note of Edward D. Sultan, Jr., dated April 27, 1949, Interest 3% per annum, due December 28, 1957 Note secured by assignment of Edward D. Sultan, Jr.'s interest in the Edward D. Sultan Trust and copartnership known as Edward D. Sultan Co. - Balance			60,782.14
			$242,497.33

Exhibit 25

Exhibit 26

Schedule of Federal Fiduciary Tax Returns Filed

	Calendar Year Ending December 31					Jan. 1st, to Sept. 30th	Fiscal Year Ending September 30		
	1942	1943	1944	1945	1946	1947	1948	1949	1950
Income									
Partnership	$24,754.29	$111,188.90	$158,396.05	$207,922.46	$103,237.57	$41,410.59	$50,711.76	$15,136.65	
Dividends	431.25	2,452.52	2,171.26						
Gain or loss on sale of capital assets			2,344.98			76.73	231.00	160.19	
Interest on government obligations						5,579.50	3,105.00	3,888.00	$4,953.00
Interest on notes								786.46	1,847.64
Total Income	25,185.54	113,641.42	162,912.29	207,922.46	103,237.57	47,066.82	54,047.76	19,971.30	6,800.64
Deductions									
Trustees fees	$ 319.10	$ 1,323.76	$ 1,734.53	$ 2,150.29	$ 1,046.98	$ 503.42	$ 564.26	$ 187.46	$ 127.95
Taxes	.33	714.81	3,809.58	2,525.92	2,571.64			253.94	
Bank charges		.45	.05					.05	.05
War damage insurance		1.65	1.65						
General postage, etc.			15.05		11.64				3.11
Contributions			1,033.20	3,693.06	3,539.34	1,222.20	4,748.10	212.10	
Adjustment of partnership income				4,200.00					
Tax service fee					50.00			100.00	100.00
Total Deductions	$ 319.43	$ 2,040.67	$ 6,594.06	$ 12,569.27	$ 7,219.60	$ 1,725.62	$ 5,312.36	$ 753.55	$ 231.11
Balance	24,866.11	111,600.75	156,318.23	195,353.19	96,017.97	45,341.20	48,735.40	19,217.75	6,569.53
Amount distributed								3,000.00	3,600.00
Net income taxable to fiduciary	24,866.11	111,600.75	156,318.23	195,353.19	96,017.97	45,341.20	48,735.40	16,217.75	2,969.53
Tax Paid	$ 9,864.35	$ 80,000.22	$121,094.62	$158,405.47	$ 60,580.20	$21,746.73	$23,142.86	$ 4,607.81	$ 500.34

[Title of Tax Court and Causes No. 24513-4.]

FINDINGS OF FACT AND OPINION

The husband-petitioner created a trust for the benefit of his minor son and conveyed to it a 42 per cent interest in his business. The settlor was not a trustee. The trustees became a special partner in a partnership in which the settlor and others were general partners for the operation of the business theretofore conducted by the petition as a sole proprietorship. One of the trustees insisted on, and received, the trust's distributive share of profits as soon as they were available for distribution.

Held, that the trust was a bona fide partner and that its distributive share of partnership profits was not income of the petitioners.

Held, further, that the settlor did not have any rights in the trust corpus or income sufficient to make the income of the trust taxable to him and his wife.

Milton Cades, Esq., and Urban E. Wild, Esq., for the petitioners.

Robert G. Harless, Esq., for the respondent.

The respondent determined deficiencies in income taxes of the petitioners as follows:

Petitioner	Year	Amount
Edward D. Sultan	1944	$145,292.17
	1945	183,632.00
	1946	60,694.17
Olga L. Sutton	1946	17,091.57

The issue to be decided is whether the distrib-

utive portion of partnership income payable to, and paid to, a trust created by the settlor and which became a special partner in the operation of a business was income to the settlor. The settlor's wife is involved only because of the community property law of Hawaii which become effective on June 1, 1945.

Findings of Fact

The petitioners are, and at all times material to these proceedings were, husband and wife, and residents of the Territory of Hawaii. Their income tax returns were filed with the Collector of Internal Revenue for the District of Hawaii. They have one child, Edward D. Sultan, Jr., (whose name was changed from Edward Dolph Sultan) born December 28, 1927.

Edward D. Sultan, one of the petitioners, and herein usually referred to as the petitioner, has been in the wholesale jewelry or jewelry manufacturing business since he was about 10 years old. In the early part of 1941, he was in the wholesale jewelry business as an individual in Honolulu. That business consisted of dealing in watches, diamonds, silverware, general jewelry lines, and everything associated with a jewelry business.

The petitioner is primarily a salesman. The manager of the business was his brother, Ernest W. Sultan, who received as compensation 25 per cent of the net profits of the business. The petitioner devoted most of his time to selling in the Far East and in the Pacific Islands. Ernest, in addition to managing the office part of the business, made some selling

trips prior to 1940. Ernest had no financial interest in the business but was very valuable to it because of his knowledge of the jewelry business.

For some time prior to August, 1941, the petitioner had been considering ways of protecting his family in the event of his illness or death, and also of interesting his son in the business. The son, who was 13 years old in 1941, was interested in the study of journalism and not in the jewelry business. The petitioner at that time was almost constantly in the care of doctors. In 1940, while the petitioner was on a trip, his brother Ernest became seriously ill and was away from the office for a few weeks.

Another brother of the petitioner, Gabriel, was a full-time salesman of the petitioner's merchandise in California. The petitioner's sister, Marie Hilda Cohen, was in San Francisco, where she and her husband owned a warehouse and they frequently supplied warehouse space for the petitioner's merchandise while it was awaiting shipment to Honolulu. In the early part of 1941, it was difficult to obtain shipping space. The petitioner's sister was a capable business woman.

The petitioner discussed with his brothers and sister possible methods of having his business carried on for the protection of his wife and son and of interesting his son in the business. He also discussed the matter with his wife, with a relative in the United States who was a lawyer, and with counsel in Honolulu. Out of these discussions there was evolved the idea of the creation of a trust and the formation of a partnership. The petitioner knew of

one instance in which a jewelry business that was in bad financial shape had been rehabilitated under the management of a trust company. He wanted a trust company as trustee of the trust to be created for his son for the benefit of the advice that it could give and for the management that it could provide in the event that he was not able to carry on the business. He wanted his brothers and sister associated with him in the business for the assistance they could give as they had in the past.

The Bishop Trust Company, Limited, an Hawaiian corporation, conducted a trust company business in the Territory of Hawaii. Its main business was the administration of estates, trusts, guardianships, agency accounts, and it acted as transfer agent, and similar business. In its fiduciary capacity, it often operated businesses in connection with its administration of estates or trusts.

On August 28, 1941, the petitioner Edward D. Sultan created the Edward D. Sultan Trust, naming as trustees Ernest W. Sultan and Bishop Trust Company, Limited. The trust instrument recited the delivery to the trustees of the sum of $42,000 by the settlor, to be used to purchase a 42 per cent interest in a partnership known as Edward D. Sultan Co. Income was to be accumulated until the settlor's son, Edward Dolph Sultan, became 21 years of age, but with discretion in the trustees to pay out not more than $3,600 per year for the maintenance, support and education of the beneficiary. Beginning at age 21, the beneficiary was to receive

$300 per month; at age 25 he was to receive a portion of the accumulated income in a lump sum. At the beneficiary's age of 30 years, the trust was to terminate and he was to receive the trust corpus, together with any cash in the estate not in excess of $20,000. Any remaining cash was to be used to purchase an annuity for the beneficiary. If the beneficiary died before age 30, corpus and income were to go to the wife of the settlor or, in the event of the happening of specified events, to the settlor's sister and brothers.

The trust instrument gave the trustees the usual powers to hold and manage the trust property, collect the income, and invest and reinvest. The trustees were not restricted to investments of the type that are permitted by law, with provisos that during the lifetime of the settlor the trustees were to obtain the settlor's consent to investments, and upon the settlor's death they were to be restricted to legal trust investments. However, the trustees could in any event make loans or advances to the partnership without liability for resulting losses. The trust was irrevocable. The corporate trustee was given custody of all money and securities in the trust estate. The settlor reserved the right to transfer additional property to the trust. Under the terms of the trust instrument neither the corpus nor income of the trust was ever to be paid to the settlor. The trust was conditioned upon obtaining court approval for the purchase of a 42 per cent interest in Edward D. Sultan Co., and approval of the trustees becoming a special partner therein. If such approval was

not obtained within 60 days, the trust indenture was to be null and void.

On August 30, 1941, a partnership was formed under the name of Edward D. Sultan Co. It was a special partnership. The general partners were Edward D. Sultan, Ernest W. Sultan, Marie Hilda Cohen and Gabriel L. Sultan. The trustees of the Edward D. Sultan trust were a special partner. The initial capital of the partnership was $100,000. Contributions of capital and partnership interests were as follows:

Partner	Contribution	Interest
Edward D. Sultan	$46,000	46%
Ernest W. Sultan	4,000	4%
Marie Hilda Cohen	4,000	4%
Gabriel L. Sultan	4,000	4%
Trustees of Edward D. Sultan Trust	42,000	42%

The partnership was to acquire the assets and carry on the business theretofore conducted by Edward D. Sultan. The general partners actively engaged in the business were to receive compensation for services rendered in such amounts as the general partners might agree on, and such compensation was to be charged as an expense in computing net profits. As long as Ernest W. Sultan was active in the business, he was to receive 25 per cent of the net profits. The remainder of the profits was to be divided in proportion to the capital contributions of the partners. The provision for Ernest W. Sultan to receive 25 per cent of the net profits was stricken

from the agreement by amendment dated June 9, 1942. Profits could be withdrawn at such time as the general partners deemed advisable.

Only the general partners had authority to transact partnership business and incur obligations. The policy of the partnership was to be established by the general partner or partners owning the majority in interest of the capital. No general partner could assign or mortgage his or her interest, but any partner could purchase the interest of any other partner. The special partner could assign its interest with the consent of the general partners.

Proper partnership books of account were to be kept. The books were to be audited periodically and copies of auditors' reports were to be furnished to each partner. Annual accounts were to be taken showing the interest of each partner and copies thereof were to be sent to each.

The partnership could be terminated by a majority in interest of the general partners on two months' written notice. Edward D. Sultan had the option to purchase the interest of any deceased general partner or of any partner who gave notice of termination. Such purchase was to be at book value without allowance for good will.

Originally the partnership was to continue until April 30, 1943, and thereafter from year to year until terminated by a general partner on six months' notice. By amendment dated February 2, 1945, the term was extended to January 31, 1946, and thereafter from year to year.

By bill of sale dated as of the close of business

on August 30, 1941, the petitioner Edward D. Sultan transferred to the partnership all of the rights, property, assets, privileges and business formerly carried on by him, having a stated value of $100,000. He received back demand notes made by him on August 28, 1941, payable to the trustees of the Edward D. Sultan trust in the amount of $42,000 and to Ernest W. Sultan, Marie Hilda Cohen and Gabriel L. Sultan, each in the amount of $4,000. He also received a 46 per cent interest in the partnership.

The required certificate of partnership and affidavits were filed and publication was duly made.

On September 5, 1941, the trustees of the Edward D. Sultan trust filed in the First Circuit Court of the Territory of Hawaii a petition to become a special partner in Edward D. Sultan Co., and to invest $42,000 in the partnership for a 42 per cent interest therein. On September 9, 1941, the court entered an order in which it instructed, authorized, and directed the trustees to become a special partner in the partnership and to invest $42,000 therein.

On or before March 15, 1942, the petitioner Edward D. Sultan filed a gift tax return for the year 1941 in which he reported a gift of $42,000 to the Edward D. Sultan trust. The respondent determined that the value of the 42 per cent interest in the partnership was greater than the reported amount of $42,000 and that additional gift tax was due in the amount of $81.99, which amount the petitioner paid.

Ernest W. Sultan managed the partnership busi-

ness until he became ill in 1942 and was required to leave the islands. The petitioner at that time took over the management. Ernest recovered quickly and, at the request of the petitioner, he opened a buying office in New York for the partnership and continued in the service of the partnership as a buyer.

The corporate trustee was given annual auditors' statements of the partnership business, and the petitioner gave it oral interim statements. The petitioner discussed business policies with officers of the corporate trustee, and conferred frequently with the other trustee on partnership matters.

The partnership made it a regular practice to pay for merchandise on the day of receipt of the invoice even though delivery to it was delayed, sometimes for months, due to the demand for shipping space and restrictions on shipment by parcel post. This practice, and an expansion of the business following the outbreak of World War II, brought about a need for more capital in the business. In order to provide the needed capital and to improve the partnership's credit rating, the partners agreed in 1942 or 1943 to leave earnings in the amount of $100,000.00 in the business to be used as working capital. This matter was discussed with officers of the corporate trustee.

The petitioner and his brother Ernest W. Sultan received compensation for services rendered to the partnership for the periods and in the amounts as follows:

Fiscal Period

Sept. 1, 1941 to Jan. 31, 1942: Edward D. Sultan,

$6,500.00; Ernest W. Sultan, $23,000.00.

Feb. 1, 1942 to Jan. 31, 1943: Edward D. Sultan, $20,431.13; Ernest W. Sultan, $95,169.99.

Feb. 1, 1943 to Jan. 31, 1944: Edward D. Sultan, $42,000.00; Ernest W. Sultan, $60,000.00.

Feb. 1, 1944 to Jan. 31, 1945; Edward D. Sultan, $42,000.00; Ernest W. Sultan, $60,000.00.

Feb. 1, 1945 to Jan. 31, 1946: Edward D. Sultan, $42,000.00; Ernest W. Sultan, $50,000.00.

Feb. 1, 1946 to Jan. 31, 1947: Edward D. Sultan, $64,000.00; Ernest W. Sultan, $15,000.00.

During the existence of the special partnership, the trustee was quite insistent on having the special partner's distributive share of profits paid over to it as soon as possible after financial statements were prepared. Payments of the trust's distributive share of the partnership profits were made to the corporate trustee as follows:

Payments Made	
June 23, 1942	$ 24,754.29
March 15, 1943	3,000.00
March 23, 1943	108,913.64
October 8, 1943	2,198.94
March 15, 1944	16,640.00
June 14, 1944	19,000.00
September 2, 1944	21,000.00
September 21, 1944	97,457.03
March 12, 1945	83,029.40
March 17, 1945	50,000.00
March 21, 1945	25,000.00
April 6, 1946	42,000.00
May 21, 1946	99,698.24

January 14, 1949	2,155.75
March 14, 1949	10,000.00
April 28, 1949	85,357.62

In 1948, the partnership business fell off, due partly to increased competition. In January, 1949, the petitioner purchased the interests of the three other general partners, namely, Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan. A formal bill of sale was executed wherein the three selling partners agreed to the termination of their interests in the partnership.

In February, 1949, the petitioner offered to purchase, and the trustees of the Edward D. Sultan trust agreed to sell, the trust's interest in the partnership. The price agreed upon, in an exchange of letters, was a sum equivalent to the capital investment of the trust in the partnership, plus the amount of the unpaid profits accumulated to January 31, 1949. At that time, the beneficiary of the trust, Edward D. Sultan, Jr., had attained his majority, and had been active in the partnership business during his summer vacations from college.

The officers of the corporate trustee gave thorough consideration to the petitioner's offer before accepting it. They were aware of the need for additional capital in the business and of the possible decrease in the business of the partnership. They decided that it would be to the best interest of the trust to sell its share of the partnership to the petitioner. The co-trustee, Ernest W. Sultan, approved the sale.

The agreement was carried out through the me-

dium of a bill of sale whereby the petitioner and the trustees of the Edward D. Sultan trust, as the "seller", sold the assets and business of the partnership to a new partnership known as Edward D. Sultan Co., in which the partners were the petitioner Edward D. Sultan, the petitioner Olga L. Sultan, and Edward D. Sultan, Jr.

The new partnership started with a capital of $250,000. Of this amount, the petitioner Edward D. Sultan contributed $127,500, the petitioner Olga L. Sultan contributed from her own funds $60,000, and Edward D. Sultan, Jr., contributed $62,500. The son, Edward D. Sultan, Jr., obtained the amount of his contribution by way of a loan made to him by the Bishop Trust Company, Limited, from the corpus of the Edward D. Sultan trust. The money was loaned on the note of the son, which note was endorsed by both of the petitioners. As additional security for the loan, Edward D. Sultan, Jr., assigned to the trust company his remainder interest in the trust and his right to monthly payments of $300 which began when he reached the age of 21 years.

The petitioner never received from the trust any of its income. During the years involved in these proceedings, the petitioner Edward D. Sultan supported his wife and son from his own income.

At August 28, 1950, the end of the last fiscal year of the trust prior to the hearing of these proceedings, the trustees of the Edward D. Sultan trust held intact the corpus of the trust estate, which consisted of the following items: cash, $9,842.58; United

States government bonds, $171,872.61; note receivable of Edward D. Sultan, Jr., $60,782.14, the total of which amounted to $242,497.33.

The Edward D. Sultan trust duly filed Federal fiduciary tax returns each year and paid the tax shown to be due thereon. The partnership, Edward D. Sultan Co., filed its partnership tax returns on an accrual and fiscal year basis ending on the 31st day of January. Its first return was filed on that basis for the fiscal year ended January 31, 1942. Returns on that basis were filed for subsequent years ending January 31, 1943 to 1949, inclusive.

By virtue of the Hawaiian community property law, which became effective as of June 1, 1945, the petitioner Olga L. Sultan was entitled to one-half of all of the income of her husband, the petitioner Edward D. Sultan, from and after that date. The entire deficiency proposed against the petitioner Olga L. Sultan arises by reason of her community property interest in the income of her husband.

The petitioner Edward D. Sultan, Ernest W. Sultan, Marie Hilda Cohen, Gabriel L. Sultan and the Edward D. Sultan trust really and truly intended to join together for the purpose of carrying on the business of Edward D. Sultan Co. and sharing in its profits and losses.

The Edward D. Sultan trust was a bona fide trust created for the benefit of Edward D. Sultan, Jr., and the petitioners did not have any substantial control over, or interest in, the corpus or income thereof.

Opinion

Arundell, Judge: The principal issue in these proceedings is whether the partnership organized under the name of "Edward D. Sultan Co." is to be recognized as a valid partnership and the income derived from its operations to be treated as the distributive income of the persons who were named in the partnerships agreement as partners. The respondent, in his determination of deficiencies, has refused to recognize the trust as a partner and has advised the petitioner Edward D. Sultan that the income received and reported by the trust is taxable to him.

The proceedings have been argued by both sides on two questions: (1) Should the trust be recognized as a bona fide partner; (2) whether the doctrine of the Clifford case* supports taxation of the trust income to the settlor of the trust.

The partnership question. The question of whether a "family partnership is real for income-tax purposes depend upon 'whether the partners really and truly intended to join together for the purpose of carrying on the business and sharing in the profits and losses or both. And their intention in this respect is a question of fact * * *' ". Commissioner vs. Culbertson, 337 U.S. 733. In the Culbertson case, the Court also said that the question of recognition of family partnerships depends upon whether "the parties in good faith and acting with a business pur-

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* Helvering vs. Clifford, 309 U.S. 331.

pose intended to join together in the present conduct of the enterprise."

The evidence in these proceedings establishes to our satisfaction that the parties to the original partnership agreement really and truly intended to join together for the purpose of carrying on the business that had theretofore been conducted by Edward D. Sultan as a sole proprietorship. The respondent, in taxing the partnership income to the petitioners, places stress on the control over the business that was in Edward D. Sultan. We had before us a similar situation in the case of Theodore D. Stern, 15 T.C. 521. In that case, the taxpayer owned the majority of the shares of a corporation. He transferred some of his shares to four trusts for the benefit of his wife and three children, dissolved the corporation, and continued the business in partnership form, in which partnership the taxpayer was the general partner and the four trusts were limited partners. It was found as a fact in that case that the taxpayer "chose to use trusts rather than transfer the interest directlyl to his wife and children so that he could retain control over the business***." In that case, we had the questions of whether the taxpayer had made completed gifts of the stock and whether the trusts should be recognized as partners in the business of the taxpayer. Both were resolved in favor of the taxpayer. On the essential facts, there is little to distinguish these proceedings from the Stern case. In that case the taxpayer was the trustee of the trusts that he created. Here, we have independent trustees, and there is evidence

that the corporate trustee was well aware of its independence and insisted on having distributed it to the portion of partnership earnings to which it was entitled under the partnership agreement. On the matter of control of the business, which remained in the settlor both in the Stern case and in these cases, we said in the Stern case:

> He retained entire control in himself but that is of no particular significance since limited partners normally have no part in the control or management of the business.

The above language was quoted with approval in the case of Bartholomew vs. Commissioner, 186 F. 2d 315, 318.

We further said in the Stern case that:

> A substantial economic change took place in which the petitioner gave up, and the beneficiaries indirectly acquired an interest in, the business. There was real intent to carry on the business as partners. The distributive shares of partnership income belonging to the trust did not benefit the petitioner.

Upon appraisal of all of the evidence in these proceedings, it is our conclusion that the trust created by the petitioner Edward D. Sultan in 1941 should be recognized as a partner in the conduct of the business and that its distributive share of the partnership income was not income of the petitioners. The factual question, as we have said, is one of intention of the parties, and this is to be resolved "from testimony disclosed by their 'agreement, considered as a whole, and by their conduct in execu-

tion of its provisions'." Commissioner vs. Culbertson, supra. There cannot be any serious question as to the valadity of the agreements in this case. Both the trust agreement and the partnership agreement were reduced to writing. The partnership agreement claerly makes the trust a "special partner" which, as we understand it, is the same, in law, as a limited partner in the States in the United States. The conduct of the parties in execution of their agreement establishes the genuineness of their intention to form a partnership. The profits of the business no longer belonged to the petitioner Edward D. Sultan. The special partner had a right to a portion of the profits and it received its portion and paid the taxes due thereon.

Both parties cite numerous cases in support of their positions. The Supreme Court has advised that family partnership cases are essentially factual. As such, previously decided cases are not particularly helpful. But a few may be mentioned for their background facts and as a help in pointing up the reasons for the conclusion we have reached in these proceedings. In most of the cases cited by the respondent, the settlors of the trusts were the trustees and had a substantial degree of control. Losh vs. Commissioner, 145 F. 2d 456; Hash vs. Commissioner, 152 F. 2d 722; Eisenberg vs. Commissioner, 161 F. 2d 506. In the case of Russell Giffen, 14 T.C. 1272, aff'd., 190 F. 2d 188, the assets placed in trust were so heavily burdened with debt that it was obvious that the beneficiaries would receive no benefit from the trust for a long period of

time. By way of contrast, in these proceedings the petitioner Edward D. Sultan definitely and irrevocably parted with a substantial portion of his business, and the income produced by that portion was no longer his. That income went to the trust company which was charged with holding and safeguarding the trust moneys and securities.

We conclude, as shown by our findings of fact, that the trust was a bona fide partner and that its income should not be taxed to the petitioners.

The Clifford case. In the Clifford case, trust income was taxed to the settlor because of the "bundle of rights which he retained." In many suceeding cases, it has been pointed out that some of the basic considerations in that case were the short term of the trust, the fact of the settlor being the trustee, the broad discretion in the settlor-trustee as to the determinaion of the income to be distributed, and the reversion of the corpus to the settlor. Here, the trust was to endure until the beneficiary who was then 13 years old attained the age of 30 years—in a period of 17 years. The settlor in these cases was not the trustee. The settlor, Edward D. Sultan, carefully selected others as trustees, and the evidence clearly establishes that the corporate trustee stood firm in its duty of protecting the beneficiary. It was insistent on having actual distribution made as soon as possible. It invested the moneys distributed to it, and at the time of the latest accounting it had a corpus in the amount of $242,497.33. In these cases there was no possibility of reversion to the settlor. None of the property or

income of the trust estate under the terms of the instrument could ever be paid to the settlor. The factual differences between the trust in these cases and that in the Clifford case are so wide as to obviate the need for any extended discussion. We hold that the decision in the Clifford case has no application to these cases.

Neither party raises the question of whether a trust can be a member of a partnership. Perhaps this is because we have heretofore decided that a trust can be recognized as a partner for tax purposes. Theodore D. Stern, supra, Louis R. Eisenmann, 17 T.C.—(Feb. 29, 1952).

We conclude that the respondent erred in including in the income of the petitioners the distributive share of partnership income of the Edward D. Sultan trust.

Reviewed by the Court.

Decisions will be entered under Rule 50.

Opper, J., dissenting: By definition the aspect of services has been eliminated in this case from the series of tests described in Culbertson.[1] That is be-

[1] "***The question is***whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise. * *** " Commissioner vs. Culbertson, 337 U.S. 733, 742.

cause a limited partner is involved only to the extent of the property committed to the venture. Theodore D. Stern, 15 T.C. 521. But if we are to look only to the property we should, it seems to me, at least be satisfied that the usual attributes of ownership inhere in its putative owner. Cf. Helvering vs. Clifford, 309 U.S. 331. Here the trust was compelled to use the alleged gift to acquire an "interest" in the business; had no control of the property; could not sell or dispose of it; could not freely withdraw profits; was confined to its investment in the partnership business; and compelled to retain that investment unless the will of the general partners, including petitioner, permitted otherwise.

As we said in Ralph C. Hitchcock, 12 T.C.22,30,31: "These documents, taken in their entirety, negative any suggestion that the petitioner, as donor, intended to absolutely and irrevocably divest himself of the dominion and control of the subject matter of his purported gifts. * * * This is not a case where the children were at liberty at any time to withdraw or assign their interests in the business or where they possessed an unqualified right to receive their full share of each year's earnings." This can scarcely be termed true ownership and eliminates the only basis on which the trust's participation in the partnership can be justified under the Culbertson tests. We have never gone so far, even in the Stern case, and I think we should not do so now. See Losh vs. Commissioner (C.A. 10), 145 F. 2d 456; Feldman vs. Commissioner (C.A.4), 186 F. 2d 87.

Hill, Harron, Le Mire and Raum, J. J., agree with this dissent.

The Tax Court of the United States
Washington

Docket No. 24513

EDWARD D. SULTAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Opinion of the Court promulgated July 3, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioner herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there are no deficiencies in income tax for the taxable years 1944 and 1945; that there is a deficinecy in income tax for the taxable year 1946 in the amount of $2,767.74; and that there is an overpayment in income tax for the taxable year 1944 in the amount of $450.00, all of which was paid within two years before the filing of the claim for refund.

Entered Oct. 31, 1952.

[Seal] /s/ C. R. ARUNDELL,

Judge.

The Tax Court of the United States
Washington

Docket No. 24514

OLGA L. SULTAN,

Petitioner.

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Opinion of the Court promulgated July 3, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioner herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there is no deficiency in income tax for the taxable year 1946, and that there is an overpayment in income tax for the taxable year 1946 in the amount of $2,060.17, all of which was paid within three years before the mailing of the notice of deficiency, which notice was mailed within three years from the time the return was filed by the taxpayer.

Entered Oct. 31, 1952.

[Seal] /s/ C. R. ARUNDELL,
Judge.

In the United States Court of Appeals
for the Ninth Circuit

T. C. Docket No. 24513

COMMISSIONER OF INTERNAL REVENUE,
Petitioner on Review,

vs.

EDWARD D. SULTAN,
Respondent on Review.

PETITION FOR REVIEW

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States in this proceeding on October 31, 1952, "That there are no deficiencies in income tax for the taxable years 1944 and 1945; that there is a deficiency in income tax for the taxable year 1946 in the amount of $2,767.74; and that there is an overpayment in income tax for the taxable year 1944 in the amount of $450.00, all of which was paid within two years before the filing of the claim for refund." This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The respondent on review, Edward D. Sultan, is an individual, whose mailing address is 1025 Alakea Street, Honolulu, Territory of Hawaii, and who was, during the taxable years here involved, a resident of Honolulu, Territory of Hawaii. The said taxpayer filed his Federal income tax returns for the calendar years 1944, 1945 and 1946, the taxable years here involved, with the Collector of Internal Revenue for the District of Hawaii.

Nature of Controversy

The sole question which was presented to and passed upon by the Tax Court of the United States is whether the income of a partnership in which the settlor-taxpayer was a general partner, and a trust created for the benefit of the taxpayer's minor son was designated as a special partner, was taxable to the taxpayer, in so far as the share thereof allocable to the trust was concerned, under the doctrine of Helvering vs. Clifford, (1940) 309 U. S. 331.

For some time prior to August, 1941, the taxpayer, Edward D. Sultan, was engaged in the wholesale jewelry or jewelry manufacturing business in the Hawaiian Islands. On August 30, 1941, a special partnership was organized in which the taxpayer, Edward D. Sultan, Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan were the general partners, and the trustees of the Edward D. Sultan Trust were named as special partner. Two days prior thereto, on August 28, 1941, the taxpayer cre-

ated the Edward D. Sultan Trust for the benefit of his minor son, naming the Bishop Trust Company, Limited, and Ernest W. Sultan, as trustees, to which trust he paid the sum of $42,000 which it was required be used to purchase a 42 per cent interest in the partnership of Edward D. Sultan Company. The taxpayer then conveyed to the partnership the assets used in his jewelry business at a stated value of $100,000 and received a 46 per cent interest in the partnership and the return to him of demand notes made by him on August 28, 1941, payable to the trustees of the Edward D. Sultan Trust in the amount of $42,000 and to Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan, each in the amount of $4,000.00.

Only the general partners had authority to transact partnership business and incur obligations.

In his notice of deficiency, the Commissioner held that the income of the partnership of Edward D. Sultan Company which had been returned in fiduciary tax returns filed by the Edward D. Sultan Trust for the years 1944, 1945 and 1946 was taxable to the taxpayer, Edward D. Sultan, settlor of the trust. The Tax Court of the United States disagreed with the Commissioner's determination and held that the settlor did not have sufficient control over the trust to make the income thereof taxable to him, that the trust was a bona fide partner in the partnership, and that its distributive share

of partnership income for each of the years involved did not constitute income of the taxpayer.

/s/ CHARLES S. LYON,
Assistant Attorney General.
/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue,
Attorneys for Petitioner on Review.

[Endorsed]: T.C.U.S. Filed Jan. 10, 1953.

In the United States Court of Appeals
for the Ninth Circuit

T. C. Docket No. 24514

COMMISSIONER OF INTERNAL REVENUE,
Petitioner on Review,

vs.

OLGA L. SULTAN,
Respondent on Review.

PETITION FOR REVIEW

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States in this proceeding on October 31, 1952, "That there is no deficiency in income tax for the taxable year 1946,

and that there is an overpayment in income tax for the taxable year 1946 in the amount of $2,060.17 * * *.'' This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The respondent on review, Olga L. Sultan, is an individual, whose mailing address is 1025 Alakea Street, Honolulu, Territory of Hawaii, and who was, during the taxable year here involved, a resident of Honolulu, Territory of Hawaii. The said taxpayer filed her Federal income tax return for the calendar year 1946, the taxable year here involved, with the Collector of Internal Revenue for the District of Hawaii.

Nature of Controversy

The sole question which was presented to and passed upon by The Tax Court of the United States is whether the income of a partnership in which the taxpayer's husband, Edward D. Sultan, was a general partner, and a trust created by the taxpayer's husband for the benefit of their minor son was designated as a special partner, was taxable to the taxpayer and her husband (on a community property basis), in so far as the share thereof allocable to the trust was concerned, under the doctrine of Helvering vs. Clifford, (1940) 309 U. S. 331.

For some time prior to August, 1941, the taxpayer's husband, Edward D. Sultan, was engaged in the wholesale jewelry or jewelry manufacturing business in the Hawaiian Islands. On August 30, 1941, a special partnership was organized in which

Edward D. Sultan, Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan were the general partners, and the trustees of the Edward D. Sultan Trust were named as special partner. Two days prior thereto, on August 28, 1941, the taxpayer's husband, Edward D. Sultan, created the Edward D. Sultan Trust for the benefit of their minor son, naming the Bishop Trust Company, Limited, and Ernest W. Sultan, as trustees, to which trust he paid the sum of $42,000 which it was required be used to purchase a 42 per cent interest in the partnership of Edward D. Sultan Company. The taxpayer's husband then conveyed to the partnership the assets used in his jewelry business at a stated value of $100,000 and received a 46 per cent interest in the partnership and the return to him of demand notes made by him on August 28, 1941, payable to the trustees of the Edward D. Sultan Trust in the amount of $42,000 and to Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan, each in the amount of $4,000.00.

Only the general partners had authority to transact partnership business and incur obligations.

In his notice of deficiency, the Commissioner held that the income of the partnership of Edward D. Sultan Company which had been returned in a fiduciary tax return filed by the Edward D. Sultan Trust for the year 1946 was taxable to the taxpayer's husband, Edward D. Sultan, settlor of the trust. One-half of such income returned by the trust was allocated to the instant taxpayer because of the Hawaii community property law. The Tax Court of

the United States disagreed with the Commissioner's determination and held that the settlor did not have sufficient control over the trust to make the income thereof taxable to him, that the trust was a bona fide partner in the partnership, and that its distributive share of partnership income for each of the years involved did not constitute income of the taxpayer and her husband.

/s/ CHARLES S. LYON,
Assistant Attorney General,
/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

[Endorsed]: T. C. U. S. Filed Jan. 19, 1953.

[Title of U. S. Court of Appeals and Cause 24513.]

STATEMENT OF POINTS

Comes now the Commissioner of Internal Revenue, petitioner on review in the above-entitled proceeding, by his attorneys, H. Brian Holland, Assistant Attorney General, and Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and hereby states that he intends to rely upon the following points in this proceeding:

The Tax Court of the United States erred:

1. In entering its decision "That there are no deficiencies in income tax for the taxable years 1944 and 1945; that there is a deficiency in income tax

for the taxable year 1946 in the amount of $2,767.74; and that there is an overpayment in income tax for the taxable year 1944 in the amount of $450.00, all of which was paid within two years before the filing of the claim for refund."

2. In failing and refusing to sustain the deficiencies in tax determined by the Commissioner.

3. In holding and deciding that the trust created by the taxpayer for the benefit of his minor son was a bona fide partner in the partnership involved and that its distributive share of partnership profits was not income of the taxpayer, Edward D. Sultan.

4. In failing and refusing to hold and decide that the trust created by the taxpayer for the benefit of his minor son was not, for Federal income tax purposes, a recognizable partner in the taxpayer's business.

5. In holding and deciding that the settlor-taxpayer did not have any rights in the trust corpus or income sufficient to make the income of the trust taxable to him.

6. In failing and refusing to hold and decide that, under the doctrine of Helvering vs. Clifford, 309 U. S. 331, the income of the trust created by the settlor-taxpayer, Edward D. Sultan, for the alleged benefit of his minor son was taxable to the settlor-taxpayer.

7. In that its ultimate conclusion that the Edward D. Sultan Trust was a bona fide trust created for the benefit of the taxpayer's minor son and that the taxpayer did not have any substantial control over, or interest in, the corpus or income of the

trust is not supported by but is contrary to its underlying findings of fact.

8. In that its opinion and its decision are not supported by but are contrary to the Court's findings of fact.

9. In that its opinion and its decision are not supported by but are contrary to the evidence.

10. In that its opinion and its decision are contrary to law and the Commissioner's regulations.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue,
Attorneys for Petitioner on Review.

Acknowledgment of Service attached.

[Endorsed]: T. C. U. S. Filed April 2, 1953.

[Title of U. S. Court of Appeals and Cause 24514.]

STATEMENT OF POINTS

Comes now the Commissioner of Internal Revenue, petitioner on review in the above-entitled proceeding, by his attorneys, H. Brian Holland, Assistant Attorney General, and Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and hereby states that he intends to rely upon the following points in this proceeding:

The Tax Court of the United States erred:

1. In entering its decision "That there is no de-

ficiency in income tax for the taxable year 1946, and that there is an overpayment in income tax for the taxable year 1946 in the amount of $2,-060.17 * * *."

2. In failing and refusing to sustain the deficiency in tax determined by the Commissioner.

3. In holding and deciding that the trust created by the taxpayer's husband, Edward D. Sultan, for the benefit of their minor son was a bona fide partner in the partnership involved and that its distributive share of partnership profits was not community income of the taxpayer and her husband.

4. In failing and refusing to hold and decide that the trust created by taxpayer's husband, Edward D. Sultan, for the benefit of their minor son was not, for Federal income tax purposes, a recognizable partner in the business of the taxpayer's husband.

5. In holding and deciding that the taxpayer's husband, Edward D. Sultan, did not have any rights in the corpus of the trust created by him for the benefit of their minor son or in the income thereof sufficient to make the income of the trust taxable to him.

6. In failing and refusing to hold and decide that, under the doctrine of Helvering vs. Clifford, 309 U. S. 331, the income of the trust created by the taxpayer's husband, Edward D. Sultan, for the alleged benefit of their minor son constituted community income taxable to the taxpayer herein and her husband.

7. In that its ultimate conclusion that the Edward D. Sultan Trust was a bona fide trust created by the taxpayer's husband, Edward D. Sultan, for the benefit of their minor son and that the taxpayer's husband did not have any substantial control over, or interest in, the corpus or income of the trust is not supported by but is contrary to its underlying findings of fact.

8. In that its opinion and its decision are not supported by but are contrary to the Court's findings of fact.

9. In that its opinion and its decision are not supported by but are contrary to the evidence.

10. In that its opinion and its decision are contrary to law and the Commissioner's regulations.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,

/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue,
Attorneys for Petitioner on Review.

Acknowledgment of Service attached.

[Endorsed]: T. C. U. S. Filed April 2, 1953.

The Tax Court of the United States
Washington

[Title of Tax Court and Causes Nos. 24513-4.]

CERTIFICATE

I, Victor S. Mersch, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 45, inclusive, constitute and are all of the original papers and proceedings, including original exhibits (1 through 39), attached to the stipulation of facts, on file in my office as the original and complete consolidated record in the proceedings before the Tax Court of the United States entitled: "Edward D. Sultan, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Docket No. 24513" and "Olga L. Sultan, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Docket No. 24514", and in which the respondent in The Tax Court has initiated appeals as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceedings, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 6th day of April, 1953.

[Seal] /s/ VICTOR S. MERSCH,
Clerk, The Tax Court of the
United States.

Before the Tax Court of the United States

[Title of Causes Nos. 24513-4.]

TRANSCRIPT OF PROCEEDINGS

No. 2 Courtroom, Federal Building, Honolulu, T. H., June 19, 1951, 9:30 a.m. to 1:00 p.m.

Pursuant to notice, the above entitled matter came on to be heard.

Before: Honorable C. R. Arundell, Judge.

Appearances: Urban E. Wild, Esq., Milton Cades, Esq. (Smith, Wild, Beebe & Cades), Bishop Trust Bldg., Honolulu, T. H., appearing on behalf of Petitioners. Robert G. Harless, Esq. (Treasury Department Counsel), appearing on behalf of Respondent. [1*] * * * * *

EDWARD D. SULTAN

Petitioner, called as a witness in his own behalf, being first duly sworn, was examined and testified as follows:

The Clerk: State your name and address for the record, please.

The Witness: Edward D. Sultan, 2942 Laola Road, Honolulu.

Direct Examination

Q. (By Mr. Wild): Are you the Edward D. Sultan who is Petitioner in Docket number 24513?

A. I am.

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(Testimony of Edward D. Sultan.)

Q. And is Olga L. Sultan who is Petitioner in Docket number 24514 your wife? A. She is.

Q. In the year 1941, Mr. Sultan, early in that year, what business were you in?

A. I was in the wholesale jewelry business here in Honolulu.

Q. Prior to that time what has been your business experience, in what lines of business?

A. I was in the wholesale jewelry business or manufacturing jewelry business practically all my life since I was ten years old.

Q. Do you profess to know any other types of businesses? [23] A. No.

Q. And what, up to that time, had been your specialty in connection with the jewelry business? Was it managing businesses or selling, or what?

A. Well, I have acted as a salesman practically since I was of age or even before that.

Q. Now when you were operating the business here as an individual, who was the manager of the business?

A. Prior to that time for some time my brother had been the manager.

Q. And what is your brother's name?

A. Ernest Walter Sultan.

Q. And he is one of the co-partners that was afterwards a co-partner with you?

A. Yes, sir.

Q. And during the time that you were operating the business as a sole proprietorship, how was he compensated?

(Testimony of Edward D. Sultan.)

A. Well, practically most of the time he received a percentage of the profits.

Q. And was that a substantial percentage?

A. Yes.

Q. And what was it in some of those early years, if you remember? A. It was 25%.

Q. Was it almost constantly that same percentage, or——

A. Yes, it was always that. I believe when he first came [24] down it was that arrangement, and he continued on that all the time.

Q. And what were his duties as manager?

A. Well, he did practically all the business and running the office and some selling, and in the office and handling the complete management of the business.

Q. Now some time in the latter part of the year or middle of the year 1941 you considered making a change in your business, did you not?

A. Yes, we had been considering it for some time.

Q. And about when did you start in considering making a change in your business?

A. I don't know exactly what you mean by the change.

Q. Well, from a sole ownership to a partnership.

A. Well, for over a year, I imagine, for some time. It was several months before that at least.

Q. And what were your purposes in mind at that time?

(Testimony of Edward D. Sultan.)

A. Well, I wanted to see that my family were taken care of, and especially to interest my son in the business. He was on a newspaper at high school and was all out for journalism, and I wanted an Edward D. Sultan & Son business later on. I had never dictated to him or propositioned him on it. I simply wanted to influence him in a way that he would naturally follow in my footsteps. [25]

Q. How old was your son at that time?

A. Thirteen years old.

Q. What, if anything, did you do concerning that desire of yours to possibly change the business and interest your son in it?

A. Well, I consulted my brother and sisters and attorneys on the manner which would be best to form a new business.

Q. And what was the reason why you decided to set up a trust with your son as the beneficiary?

A. Well, a trust would still give him a partnership and finally obtain the interest in the business that I wanted him to have, and it would protect him and the family in case of my death or illness, and also I was impressed with the benefits that a trust could give in the way of advice and the management in a business providing I would be out of the picture, or even while I was in the picture.

Q. Well, what was your own health about that period of time when you were contemplating the formation of this trust?

A. Well, I was almost in the constant care of

(Testimony of Edward D. Sultan.)

the doctors and had been going down quite a good deal. That was one of the reasons why I wanted to do something about it very soon.

Q. And you said something about you wanted to get the benefit of a trust company in the management. Had you had knowledge of that in your own line of business before? A. Yes. [26]

Q. What was that knowledge?

A. The Joseph Schwartz Company here, a wholesale jeweler, had been in the hands of a trust company, and when they took it over I understood that it was in bad shape with a poor rating, and it developed to a good rating and a very substantial business under the management of the trust company.

Q. Was that Joseph Schwartz Company one of your competitors? A. Yes.

Q. Now, in the discussions leading up to the preparation of the deed of trust, did you consult with a counsel on that? A. Yes, indeed.

Q. And at that time what advice, if any, were you seeking?

A. Well, I wanted to know the best way of obtaining the objective I was after, and naturally I went to him to learn that way, to see what he thought.

Q. And what was that objective that you were after that you just referred to?

A. Well, I wanted to protect the family in case of illness, the wife and son, and to interest him in the business.

(Testimony of Edward D. Sultan.)

Q. Were those your only objectives at that time?

A. Yes, sir.

The Court: How would this protect the wife?

The Witness: Well, I believe that we made some provision in case of his death that she would have it, something to do with the business. It is a matter of record, I [27] believe.

The Court: All right, proceed.

Q. (By Mr. Wild): Now, at that time did you yourself say, "I want to set up something to relieve me of the burden of taxes" to your counsel?

A. No, sir.

Q. Did you have a motive of tax avoidance in mind at that time? A. No, sir.

Q. Was that at all considered by you as a factor in determining what course you wanted to pursue?

A. I imagine it was discussed later on, but it wasn't considered by me as to the setup we would have. I wanted something that would assure the protection of the family.

Q. Now, at the precise time you had this under consideration did you have conferences with your brother Ernest, who was the manager of your business, to get his viewpoint on it?

A. Yes, many times. I took everything up with him. It wasn't really a tax problem at that time. We weren't making that kind of money.

Q. Will you explain why you say there was not a tax problem at that time?

A. Well, it was before the war, before the real activity had started here, and although our busi-

(Testimony of Edward D. Sultan.)

ness was gradually increasing, we were, for instance, placed on a quota basis [28] with our biggest supplier, a line that we had depended principally on, and that quota was less than the amount we had obtained previously from them, which meant that our volume would be cut down a great deal, and other suppliers put us on a quota basis. There was a shortage of many materials for our business, even as late as the middle of 1941.

Q. What were the outlooks for continued source of supply, to meet the demand for the products which you wholesaled at about the time you were considering the formation of the partnership?

A. Well, when we first started considering, I imagine that the supplies were fairly ample, but they became tighter all the time, and by the formation of the partnership we were still obtaining quite a little goods, but the indications later on or even then were that we would be cut down a great deal in our supplies.

Q. Now, you had besides your brother, Ernest Walter Sultan, a sister, Marie Hilda Cowen, and where was she located at that time?

A. In San Francisco.

Q. And she had anterior experience in the jewelry business? A. No.

Q. What had been her line of business?

A. Well, she and her husband run a radio business in San [29] Francisco, and they had a warehouse and a shipping department and in many cases it warehoused our goods, and previous to that my

(Testimony of Edward D. Sultan.)

brother had sold our line and during that time was selling our line on the mainland, a line of Hawaiian goods.

Q. By that brother, do you mean Ernest Walter?

A. No, the other brother, Gabe Sultan.

Q. But was it necessary at about that time to have warehousing space in San Francisco in the conduct of your business? A. Yes.

Q. And why was that, Mr. Sultan?

A. Well, sir, shipping was a very difficult thing at that time, shipping to the islands. The pre-war demand for space of necessary materials was already in effect, and we couldn't get the shipping space.

Q. In brief, that was a period when we were building up armaments and defenses here, is that right? A. Yes, sir.

Q. And shipping space was prorated for the defense endeavor, is that right?

A. I don't know if it required a priority at that time. I don't recall, but shipping was very difficult to be able to obtain. It was very difficult. And to be able to obtain goods which were on a quota basis, we bought them and sometimes warehoused them in San Francisco waiting space to the [30] islands.

Q. Now, your brother, Gabriel Louis Sultan, where was he located?

A. In San Francisco also.

Q. At that time he was there?

A. Yes.

(Testimony of Edward D. Sultan.)

The Court: He is the one you are talking about, isn't he?

The Witness: No, my sister and her husband were the ones that had the warehouse.

Q. (By Mr. Wild): And prior to that time he had acted as salesman for you, you said?

A. Yes, sir, full-time salesman on the road around California.

Q. A full-time salesman? A. Yes, sir.

Q. Now, what was the nature of your business at that time, Mr. Sultan?

A. Well, it was still associated with the jewelry business, and we imported pikake shells, which is a souvenir item here, and we remanufactured them here in the islands into necklaces, and so forth, and he sold them in the resort places in California.

Q. And were you a wholesale jeweler or what at that time?

A. Yes, sir, we carried everything in jewelry.

Q. Just describe the business for the Court.

A. Well, we bought watches and diamond goods and general jewelry lines, and silverware, practically everything associated with the jewelry business, because here we have a very complete line. We have such a small territory. We have bought and sold to other retail jewelers and other retailers who carried those goods, at a profit.

Q. Now, do you recollect a petition having been filed in court asking for authority by the trustees to accept the gift for the trust of an interest in your business in the partnership?

(Testimony of Edward D. Sultan.)

A. Yes, sir, I attended the hearing.

Q. You knew about that? A. Yes, sir.

Q. Very well. As a result of the hearing, the stipulation shows that the Court approved the investment and the deed of trust was conditioned upon that approval, and so after that then the partnership became really operative, is that right?

A. Yes, sir.

The Court: It is a trifle leading, but I guess it is all right.

Mr. Wild: Well, it is sort of hard, your Honor, when we are tied up to a lot of exhibits. I apologize. I didn't mean to be leading. [32]

The Court: That's all right. Proceed.

Q. (By Mr. Wild): Now, Mr. Sultan——

The Court: The point I was thinking about, that whole line of testimony, if there is any significance to this court action. It seems to me we ought to get something as to how that was done, whose idea was it? I can't believe it is this witness's idea, unless he knows a good deal more about law than people usually do.

Mr. Wild: No, he doesn't. He doesn't purport to. Might I just make a brief statement, your Honor? I believe that this was the first time that the issue, the question of an inter vivos trust to be handled by a corporate trustee in an active business, not as a fiduciary of a deceased's estate, but in an inter vivos trust, had come up, and that the trust company with due precaution, and I believe on advice of counsel, filed a petition, feeling it was

(Testimony of Edward D. Sultan.)

good business from a business standpoint, setting forth to the Court, and after hearing evidence there was a decree granted. Had that not been done by the provisions of the trust deed itself, as I read it, the trust would have terminated. But once that hearing had been had within the period of time and the Court had approved the action and the trust went into full effect and continued. But this witness, your Honor, he just knows about it, that's all. We don't assume that he knows the legal significance of it at all. [33]

Q. (By Mr. Wild): Now, Mr. Sultan, your brother, Ernest W. Sultan, acted as the manager of the partnership business at the outset, you have heretofore testified? A. Yes, sir.

Q. How long did that management of the business continue by him?

A. Well, he became very sick again toward the middle of 1942, and he was at such a point that he was required to leave the islands, and at that time he withdrew from his arrangement and went up to the coast, and I took over the management of the business and employed or tried to employ various office managers there, with some success at different times. Then, my brother, feeling better on the coast, opened an office for us in New York and operated that as a buyer for us where we found the necessity after the middle of 1942.

Q. So that actually at that period of time he was able to resume active duties for the partnership? A. Yes, sir.

(Testimony of Edward D. Sultan.)

Q. Within a very short period of time?

A. Yes, sir.

Q. Now, during these years of operation, take the first period ending January 31, 1942, from September, 1941, did you draw compensation for your services? A. Yes sir. [34]

Q. And do you recollect what the amount of that was? A. About $1,300 a month.

Q. And was that charged as an expense before profits were computed?

A. Yes, sir.

Q. What was your brother's compensation as manager?

A. It was 25% of the net profits of the business before any division, and he received that, and I received my salary, after which we made the division of the profits on a percentage basis.

Q. Now, do you have there the amount which you received for the fiscal year ending January 31, 1943, 1944, 1945, 1946, and so forth?

A. Yes, sir.

Q. Will you please testify as to what amounts you received for personal services during those periods?

Mr. Harless: Wait a minute; what is he reading from and where did it come from?

Q. (By Mr. Wild): What are you reading from, Mr. Sultan?

A. I am reading— Here, I will read from this slip, which is the figures furnished to me by our bookkeeper.

(Testimony of Edward D. Sultan.)

Mr. Wild: I asked Mr. Sultan to have these figures and be prepared to testify to them.

Mr. Harless: All right, I just wanted to see what it was [35]

The Witness: The five-month period from September 31 should be from September 1—I think this is an error, Mr. Wild—it should be September 1, 1941. This says September 31. Yes, it should be September 1, 1941, to January 31, 1942, was $6,500. From February 1st to January 31, 1943, was $20,-431.13. The next fiscal year was $42,000. The next was $42,000. The next was $42,000 and the one starting in 1946 was $64,000. The one starting February 1, 1947, was $74,000 and the one starting February 1, 1948, $64,000.

Q. (By Mr. Wild): Now, those amounts were paid to you by the partnership, Edward D. Sultan Company, for your services to the company?

A. Yes.

Q. Do you consider the amounts that were paid as ample compensation for your personal services?

A. Yes, sir.

Q. And those amounts in each instance were paid as expenses of the partnership business before any division of profits, is that correct?

A. Yes, sir.

Mr. Wild: I think I gave you a copy of Ernest's withdrawals also. [36]

Mr. Harless: Yes.

Mr. Wild: That is 9-1 instead of 9-31.

Q. (By Mr. Wild): Now, your brother, Ernest

(Testimony of Edward D. Sultan.)

W. Sultan, as manager also drew compensation during these periods. Will you state what those were?

A. Yes, sir. This was on the agreement that we had?

Q. Yes, the agreement.

A. From September 1, 1941, to January 31, 1942, $23,000. The next fiscal year from February 1 to January 31, 1943, $95,169.99. The fiscal year ending January 31, 1944, $60,000. At that time his old agreement expired and his new bonus and salary were settled on each year. The following year ending January 31, 1945, $60,000. Ending January 31, 1946, $50,000; and ending January 31, 1947, $15,000. He had retired and closed our New York office, I believe, in May or June of that year.

Q. And that compensation was for the period that he was operating that office? A. Yes, sir.

Q. What have you to say as to whether that was compensation adequately compensating him for personal services to the business during those periods?

A. It was very adequate.

Q. Were these items of payments in his case deducted actually before determining net profits divisible to the [37] partners?

A. Yes, both his and mine were deducted before division of the profits.

Q. Now, with the impact of December 7th and the war, were there serious changes made in your business here, Mr. Sultan?

A. Yes, sir; almost immediately after the war it looked as though we would practically have to

(Testimony of Edward D. Sultan.)

close up. We didn't know what shipping we would receive or what materials we would receive, but after a few months the velocity started of the thousands and thousands of people that were sent down here to the islands, and the fact that we had certain quotas that we were able to make, the business grew very rapidly from there on. It was because of the conditions becoming so different than they had been.

Q. Well, what would you say about the growth of your business during that period? Was it one that you had expected theretofore?

A. As I say, right after the war, immediately after the war we thought we would be out of business, so the growth of the business during 1942 and especially 1943 and I believe 1944 was our biggest year, were entirely unexpected at that time.

Q. Will you tell us something about your buying problems at that time?

A. Well, because of the buying problems I urged my brother to open the office in New York, which he did. I believe it was in the summer, August or September of 1942. We had a good rating and we wanted to keep it, and we paid our bills the minute any shipments were made to us, which eased our buying problem somewhat, but we were constantly back at the factories trying to obtain commitments for goods to us.

Q. Well, will you kindly explain that? What was the method then that was commenced in acquiring stock from the factories?

(Testimony of Edward D. Sultan.)

A. Well, we would go back to the factories, which was almost necessary, and place our orders, and they shipped—the shipments were made direct to Honolulu and invoices were sent to our New York office. We established an account in New York and kept our money there, and my brother paid for these goods the day the invoice arrived from the factory to our New York office, the duplicate invoice, and in 99% of the times it was paid on the day we received the invoice, in order to have the factories be favorable toward us in giving us more merchandise, which we needed badly.

Q. Now, how long would it be before you would get the merchandise that you purchased? Would that come through normally rapidly, or would it be delayed?

A. Well, it depended upon priorities that we would have here. If they were a large amount of goods and we would receive a very small priority the goods, especially freight, they would lay in San Francisco waiting until we got the [39] proper priority or until the priority we had would bring them to the islands. If they were parcel post, we were restricted to eleven pounds a week from any one shipper, which was the law here at the time, to any one consignee, and in many cases an order of boxed jewelry or something else would take three, four or five months for the factory to be able to fill that order, but they would bill us for it the minute the shipment was ready and we would pay for it, and

(Testimony of Edward D. Sultan.)

that would take care of the eleven pounds a week coming to us, unless we were able to get a priority, which was unusual in our business.

Q. Now, in connection with that development in your business, did you do anything about getting these other partners to agree to leave a part of their earnings in the partnership business?

A. Well, we always left our earnings in there until we needed them because we needed the money in the business and we needed to keep large cash deposits in New York to pay for anything that we could possibly get immediately, and except for the trust partner, why we would leave our money in the business for some time until profits and collections on the new year had caught up with us, so that we could pay our taxes and profits.

The Court: What about these big salaries? Did you draw those out of the business? [40]

The Witness: No, sir; they were credited, I believe. I believe I drew $2,400 a month, and my brother had a drawing account. He drew what he wanted.

The Court: I mean did you take this $2,400 a month out of the business?

The Witness: Yes, sir, it was taken out of the business and credited to my personal account, I believe, and the bonuses over the $2,400 a month were paid to me as soon as we had ample funds, which usually was several months after the next year. I believe our bookkeeper took care of the

(Testimony of Edward D. Sultan.)

income tax, which was a great portion of what my earnings were.

Q. (By Mr. Wild): Now Mr. Sultan, in about sometime the end of 1948 or early 1949 there had been radical changes in the business, had there not?

A. Yes, sir.

Q. Will you describe those for the Court, the conditions and what had happened?

A. In the fall of 1948 we had a very serious strike here. Our volume dropped considerably and and our collections became very slow, and it was a very unhappy period, as far as I remember.

Q. Well, what happened as a result of that?

A. Well, we just simply—our business declined a great deal. [41]

Q. At that period of time did you consider reorganizing the business, terminating the special partnership and doing anything about that situation?

A. Yes, I was in constant touch with my brother, and I had a very unfortunate experience in the jewelry business before that, and I knew that our accounts would slow up a great deal, and that in order to continue I would have to have more money in the business, and consequently my brother and sister were very happy to sell out, as well as the trust company, and so we re-established the business.

The Court: I don't quite follow that. You say that the business needed more money?

The Witness: Yes, sir.

(Testimony of Edward D. Sultan.)

The Court: And what you do, as I get it, is you buy out some partners, which doesn't give the business more money but takes money from the business.

The Witness: I had been continually loaning the business large sums of money myself, without interest in fact, and we were under-capitalized. We were capitalized for $100,000 where we needed at least a quarter of a million dollars or one-third of a million dollars in the business. The trust company had insisted on their money. In fact, many times they would call me and say, "When are you going to send us our check, and where is our statement", and what not, and so we paid them off as promptly as we possibly [42] could, which the books will show, and we didn't have enough money to continue by paying off the profits that way. So we were under-capitalized three to one.

The Court: I understand that, but I don't understand how what you did gives more capital to the business. You say you bought out your brother and sister and you buy out the interest of the trust. Now that doesn't give you more money.

The Witness: We took in more money from my son than we had paid out to the trust company, a substantial amount more, and also a substantial amount from Mrs. Sultan, and I also put in more money, so we recapitalized for a quarter of a million dollars instead of $100,000.

The Court: All right, go ahead.

(Testimony of Edward D. Sultan.)

Mr. Wild: I was just going into that with him, your Honor.

The Court: All right.

Q. (By Mr. Wild): In the changed years with the strike and all that, had that affected the rapidity of collections in your business? A. Yes, sir.

Q. And what had that effect been?

A. Well, the collections had slowed up a great deal, which is a matter of record on our books. Our turnover had dropped considerably. [43]

Q. And prior to this time had your son become interested in the business? A. Yes, sir.

Q. What had been the courses which he had pursued in school?

A. Well, originally, even up to college, when he started at Stanford, he started with a journalistic course. He came down here and worked the first summer during his vacation and worked for us, started in the bookkeeping and the shipping room and became very interested. He changed his course to business administration and continued on in that, and graduated in the business administration course, and each summer he came down and worked in the office.

Q. And did he desire then to participate in the active management of the business?

A. Yes, sir.

Q. And was that one of the things you had in mind when you desired to buy out your brothers and sister and buy out the trust interest in the business and add more capital to it?

(Testimony of Edward D. Sultan.)

A. Yes, I always had in mind that I wanted him in the business as a partner of mine.

Q. And actually did that occur?

A. Yes, sir.

Q. Was this extra capital put in the business?

A. Yes, sir.

Q. You did that even though you felt conditions were bad [44] at that time? A. Yes.

Q. Why was that?

A. Well, I don't know, I wouldn't know which way to turn except the jewelry business, and when conditions are fairly good it is a good business. I wanted to continue it and to continue it so my son would continue after me.

Q. In short that is the only business you know, is that right? A. Yes, sir.

Q. And you felt the time had come for more capital? A. It was very necessary.

Q. How long did your son actively then engage with you in the business?

A. He graduated from college, I believe, in June, 1949, and I believe he started to work in the office in July 1st, 1949. And he had three summers, I believe, in the office and started out as I had started as a fairly young boy out selling and becoming acquainted with the trade. He knows every jeweler in the Hawaiian Islands, and he is associated with me, and it is understood by everyone that he is going to be in the jewelry business and take over my business.

Q. Where is he now?

(Testimony of Edward D. Sultan.)

A. He is in the United States Army, Fort Ord, California, leadership school. [45]

Q. How long has he been there?

A. Six to seven months. He has been in the army six to seven months, at Fort Ord about four months or three months.

Q. Was that because he was dissatisfied with the jewelry business?

A. No, sir; he was inducted into the army.

Q. Do you know what his present aims are?

A. His present aims are that he wants to be in the jewelry business back in Honolulu.

Q. Now, Mr. Sultan, during the period of time that you had a special partner that was the trust and your brother and Bishop Trust Company as trustees, did you consult at all with them as trustees concerning business policies?

A. Yes, sir.

Q. And with whom did your consultations take place in the trust company, for instance?

A. Well, Mr. White, and later Mr. Benner.

Q. And by Mr. Benner you mean Mr. Edwin Benner, Jr.? A. Yes, sir

Q. How long have you known Mr. Benner, Mr. Sultan?

A. I think about since the trust was established.

Q. Did you furnish them regularly with accounts of the conduct of the business?

A. Yes, sir.

Q. And how often were those accounts furnished? [46]

(Testimony of Edward D. Sultan.)

A. We furnished them an annual auditor's statement every year, gave them one for their records. We turned it over as soon as the auditor furnished us with it.

Q. And did you give them interim accounts?

A. Only by discussion, I believe. I don't believe we had interim accounts.

Q. Did they confer with you over the course of your business, what was happening there?

A. Yes, they did. We were becoming more successful all the time, and they were quite satisfied. We weren't in there terribly often because everything was going so beautifully in a business way.

Q. The other co-trustee, your brother, was then actively engaged in New York? A. Yes, sir.

Q. Handling the buying?

A. Yes, and I spent sometime in New York each year also helping him. That was a big part of our work there. I conferred with him constantly on everything.

Q. During the period of your son's minority up to the time that he arrived at the age of twenty-one, who supported your son and wife?

A. I did.

Q. Out of what moneys?

A. Out of my own money. [47]

Q. Did you or did you not receive any moneys from the trust? A. No, sir.

Q. For their support?

A. None at all.

Mr. Wild: No further direct.

(Testimony of Edward D. Sultan.)

Mr. Harless: If the Court please, I wonder if we could ask for a recess now, and we will get these returns fixed up.

The Court: Very well, we will take a brief recess.

(Recess.)

Mr. Wild: Might I ask the indulgence of the Court and counsel to ask one or two additional questions?

The Court: Very well.

Q. (By Mr. Wild): Mr. Sultan, at the time of the partnership being formed in 1941, did you then execute a will naming a fiduciary?

A. Yes, sir.

Q. And who was the trust company named as the fiduciary in the will, Bishop Trust Company, Limited?

A. They, with my brother Ernest.

Q. A little while ago in response to a question asked by the Court as to how the trust protected your widow, you said she was an alternate beneficiary with your son in the event of his death. Did you also have any other thing in [48] mind as protecting your wife?

A. Well, except that I wanted to have the executors acquainted with the business so it could continue and protect her in that way, and if anything happened to my brother, why the Bishop Trust Company have been familiar with my business and along with the help of our office could run it and protect her in that way.

(Testimony of Edward D. Sultan.)

Q. You say protect her. Was she a beneficiary? Would she have been a beneficiary under your will had you died and she outlived you?

A. Yes, sir.

Mr. Wild: No further questions.

Cross-Examination

Q. (By Mr. Harless): Mr. Sultan, isn't it a fact that on or about August 28, 1941, you executed certain notes to your brother Ernest, your brother Gabriel and your sister Marie and the Bishop Trust Company and Ernest as trustees for your son?

A. Yes, sir.

Q. Did you actually prepare those notes?

A. Yes.

Q. Did you deliver them to the persons named in there as the payee?

A. I believe so, yes.

Q. Did you deliver those notes on condition that they be [49] returned to you in the purchase of an interest in a partnership either then created or to be created?

A. I don't remember if that was one of the conditions or not.

Q. Why did you give the notes?

A. Well, I didn't have the cash on hand, I guess. I didn't want to take it right out of the business at that time.

Q. Isn't it a fact that you did give these notes for the purpose of permitting these people to in-

(Testimony of Edward D. Sultan.)

vest the notes back in the partnership? You gave the notes instead of cash?

A. My primary reason with my son was definitely I wanted him in the partnership, and I wanted—Yes, I imagine the answer is yes to that question. I wanted all of them in the partnership.

Q. Why did you give notes to your sister Marie Cowen and your brother Gabriel? Why did you want them in the partnership?

A. Both of them had been associated with the business, and I wanted them. My sister is a capable business woman. My brother had been associated in the business before too, and if we could keep them that way it would give added protection to the business.

Q. How was Marie Cowen associated with the business prior to the formation of the partnership? [50]

A. Well, we handled shipments from San Francisco, I believe, and stored stuff in her husband's warehouse.

Q. She was in the radio business, wasn't she?

A. Yes.

Q. You weren't in the radio business?

A. Yes, sir.

Q. I believe you testified on direct that Mr. Gabriel Sultan was a mainland salesman for your firm. A. Yes, sir.

Q. Was that true prior to the formation of the partnership in 1941? A. Yes, sir.

Q. That continued after that time?

(Testimony of Edward D. Sultan.)

A. It was eliminated because we couldn't get the supplies to furnish him and we did not need to sell it up there.

Q. He no longer performed any service for the partnership or was not employed by the partnership, is that right?

A. No, sir.

Q. Then this partnership interest to your brother Gabriel and the accumulations thereon amounted to either a pure gift or some recognition for services rendered in the past to you, is that correct?

A. Well, the intent that was entirely different. The circumstances brought that about, yes, brought about the fact that his investment in our business paid him [51] substantial dividends.

Q. What was his investment, your note, isn't that right?

A. Well, that was an investment. It was satisfactory to the government before.

The Court: I don't get that answer. Read it, please.

(The answer was read by the reporter.)

The Court: I don't understand that answer.

The Witness: At the time they originally questioned the trust they questioned Ernest, Gabe and Marie's investment also, and at the local Internal Revenue Mr. Peterson was satisfied to eliminate any claim on their profits.

Q. (By Mr. Harless): I am not arguing about that, Mr. Sultan. All I want to know is just what it was your brother and sister put into this thing,

(Testimony of Edward D. Sultan.)

or what was the reason for the note you gave them. What was the consideration?

A. The first consideration was to have them interested in the business.

Q. Why? They weren't going to contribute any thing to it? A. They both had functions?

Q. Were they to function after the partnership started?

A. Yes, they were to function depending on conditions.

Q. Now as far as the note to the trust is concerned, that again was a gift, is that correct? [52]

A. Yes.

Q. There was no money involved?

A. Well, I gave a note that is worth $42,000.

Q. But you gave the note contingent upon the trust purchasing an interest in this alleged partnership, didn't you?

A. That was discussed and brought about in that way, yes.

Q. Discussed with whom?

A. With my advisors, the attorney, and so forth.

Q. Who were your attorneys?

A. My attorney? Mr. Cades.

Q. Did they advise you to do it that way?

A. I believe so, yes.

Q. Did they advise you to set up this trust and put it into a partnership?

A. Well, it came about after a lot of discussions. I have a cousin in Philadelphia whose advice I take a great deal. He discussed it with me. I have

(Testimony of Edward D. Sultan.)

discussed it with my brother, with my wife, and it came about over a long expanse of time.

Q. Who finally determined that it should take the form that it ultimately did take?

A. It was determined at meetings.

Q. By whom?

A. I really can't say. [53]

Q. You were there, weren't you?

A. Yes. It was determined by mutual consent.

Q. Of whom?

A. Of myself, the attorneys and my brother and everybody else concerned.

Q. Prior to the formation of the partnership, what interest did your brother have in your business?

The Court: Which brother? Let's get them straight.

Q. Brother Ernest.

A. No financial interest.

Q. He had no financial interest?

A. Yes.

Q. He was an employee, was he not, on a bonus arrangement?

A. Yes, sir. He was the backbone of the business, very valuable to the business. His knowledge was far, I believe, above mine.

Q. He was still an employee, was he not?

A. Yes, on a profit participating basis.

Q. And isn't it a fact that after the formation of the partnership Ernest Sultan's relationship to the business remained almost the same, both as to

(Testimony of Edward D. Sultan.)

compensation and activity, up to the time he became ill? He still got 25% of the net profit?

A. Yes.

Q. He still participated and managed, isn't that right? [54]

A. Yes, sir, he managed it.

Q. Was there any discussion between yourself, your brother Ernest, your brother Gabriel, your sister Marie and the trust company as to Ernest's place in this arrangement? A. There was.

Q. In which he continued to get 25%?

A. Yes, it was always assumed he would continue on that basis.

Q. Was your brother Ernest willing to participate in this arrangement if he didn't get the 25%?

A. Well, I don't know. I never tried to chisel him down.

Q. It wasn't a matter of chiseling. Were there any discussions that that was his share?

A. You tell a man you are going to give him so much, and after he has worked for awhile you say, "I am cutting you down", he should accept it? I don't know.

Q. Did you tell him his treatment would be the same under the partnership as it had been theretofore?

A. Yes, except that he would get the benefit of his profits on the partnership.

Q. What was his interest in the partnership?

A. Four percent.

Q. Now you testified that your reason for set-

(Testimony of Edward D. Sultan.)

ting up a trust for your son and conditioned its further existence upon its coming into the partnership was for the purpose of interesting a thirteen year old boy in the business?

A. Yes, sir.

Q. Is that correct? A. Yes.

Q. What, at the time you created the partnership, did you think that either your son or the trustee of the trust could contribute to your business?

A. The trustee, the Bishop Trust Company?

Q. The Bishop Trust Company and Ernest Sultan?

A. I was sure that Ernest Sultan could participate if he was well, and he can handle the business until my son became of age. The trust company, I wanted to have them familiar with it because I know they have run many businesses here in the islands, and they certainly can take over. They couldn't take over our business without experience in it.

Q. Now was Ernest Sultan interested on his account as a co-trustee or because he had a very substantial interest as an individual? Was he rendering his time on his own account or as a co-trustee?

A. Rendering what?

Q. His time to the business, his efforts, his work?

A. He was rendering his time as an employee of the firm, I imagine. [56]

Q. As a partner?

A. As a partner, yes, sir.

(Testimony of Edward D. Sultan.)

Q. How great, or do you know how much interest——

A. He had also his interest as a co-trustee and was kept informed in that way.

Q. Do you know how you could separate his activities between his individual concern and his interest as a co-trustee?

A. No, I don't. I know he was 100% for both, and sincere.

Q. Do you know how often he conferred with the other trustee, the Bishop Trust Company relative to your policies in the business?

A. Well, up to June, 1942, which was almost a year, I know he was over there very often.

Q. Did he receive any compensation as a co-trustee?

A. No, sir; I don't believe so.

Q. You testified regarding the managership of the business prior to the creation of the partnership, and I believe you stated that your brother Ernest had been very active in managing that business while it was a sole proprietorship, is that correct?

A. That is correct.

Q. At that time what were you doing in the business?

A. I was out selling generally most of the time.

Q. On the mainland or here? [57]

A. I covered the Far East and here. I covered the outside islands.

Q. Did he too take trips?

(Testimony of Edward D. Sultan.)

A. Yes. The business was small enough so that both of us did some selling.

Q. You divided the responsibilities of management then?

A. No, sir. Yes, I was consulted all the time, but he ran the business. He was in the office most of the time.

Q. It was still your businss so that you had the right to veto things he did, or approve them, is that correct? A. Yes, certainly.

Mr. Wild: Might I ask what period of time that last question referred to?

Mr. Harless: Prior to the formation.

Q. (By Mr. Harless): After the formation of the partnership, Mr. Sultan, Ernest continued to be most active in managing the business up until the time of his illness, is that correct?

A. Yes.

Q. Were you outside selling at that point too?

A. Yes, practically all the time.

Q. Was he also doing a considerable amount of traveling?

A. No, he didn't travel at all after—In fact, the last year, since 1940, he didn't travel after his first illness. [58]

Q. He had been ill?

A. Yes, in 1940 he was very seriously ill here in Honolulu, while I was away on a trip.

Q. Who managed the business while he was ill?

A. He managed the business.

Q. While he was sick?

(Testimony of Edward D. Sultan.)

A. While he was sick. He was away from the office a few weeks, and it continued to function. I was away also. I didn't know about it until my return.

Q. Now after the formation of the partnership in August, 1941, you had a 46% interest in that business, is that correct? A. Yes, sir.

Q. And as such you are described in the partnership instrument as the majority general partner in interest, is that correct? A. Yes, sir.

Q. Isn't it true that the provisions in the partnership agreement give you complete control of the partnership business?

A. Well, I don't know how complete control I have. I never took complete control.

Q. You could have exercised it.

Mr. Wild: May it please the Court, I think that calls for an opinion of a legal expert, and we haven't [59] qualified this witness as such.

Mr. Harless: It is his partnership agreement. He ought to know what he can do under it.

The Court: Well, I don't think it is too important, but I think I will overrule the objection. Answer if you can; if you can't answer, just say you don't know.

The Witness: I really don't know 100%.

The Court: All right.

Q. (By Mr. Harless): Have you ever read that partnership agreement? A. Yes.

Q. When was the most recent reading?

A. It has been quite sometime.

(Testimony of Edward D. Sultan.)

Q. Did any of the other partners have a right to terminate the partnership?

A. Yes, all of them did, I believe.

Q. How could that be done?

A. Well, the end of the first—They could terminate it practically any time after the first period of about a year, a little over a year, and then we made an amendment, I believe, so that it would have to be determined in case of the death of one of the partners or desire to terminate, why it would run until the end of the fiscal year.

Q. But weren't there certain options left to you, Mr. Sultan, to purchase the interest and keep the business going? [60]

A. I am pretty sure it was, yes.

Q. Were those same options given to any other partners in this business?

A. I don't think so.

Q. What happened to the business in case you died?

A. My portion of the business went to my estate, and the Bishop Trust Company as executor to my wife's will would continue to operate the business, as I understood it.

Q. Didn't your personal representative, on your death, have an option to determine whether or not to continue your interest in the business or not?

A. I don't know. I don't think he did.

The Court: You mean given by the instrument or just as a matter of law?

(Testimony of Edward D. Sultan.)

Mr. Harless: No, it is by the instrument, your Honor.

Q. (By Mr. Harless): Were the partners entitled to withdraw their profits from the business at will?

A. I don't know about the co-partners. I believe they were. I know the Bishop Trust Company were the toughest collectors we had.

Q. Was the special partner entitled to draw any profits from this business? A. Yes, sir.

Q. Entitled to, I say, entitled to draw any profits from [61] this business without your consent?

A. I don't know. I didn't think so.

Q. Isn't it a fact that the Bishop Trust Company, as co-trustee, wrote a number of letters to the alleged partnership asking for funds so that they could pay the taxes?

A. I don't remember that. I know we paid them off before anyone else was paid off, and in some cases we had to wait until certain commissions came in to do it.

Q. It took some time on occasion?

A. Very seldom any time. It was paid off except for a short period where we made an agreement to leave them in for a little over a year, to leave an equal amount as their original investment in the business as part of their profits. Outside of that they were paid off in cash two months to four or five months. Practically always when the auditors furnished us with his report.

Q. Now getting back for a moment to the mat-

(Testimony of Edward D. Sultan.)

ter of the preparation of the partnership agreements and the discussions which you testified you had with any number of persons, isn't it a fact that the partnership and the trust documents were prepared by your present counsel in this proceeding?

A. Yes, sir.

Q. And isn't it a fact that the documents, the trust document and the special partnership agreement, together [62] with the amendments, the entire arrangement was suggested by your present counsel?

A. Not suggested. During our discussions he certainly was in accord with it.

Q. Now who did suggest that you have a trust, did you?

A. As I said before, there was many discussions on the thing.

Q. Who finally came up with the idea that you would set up a trust and have it take a partnership interest? That is quite a complex arrangement.

A. I don't know if it originated in the East, with this attorney cousin of mine or not, or it might have originated here. I wanted some manner of protecting my son and family and I didn't want him to receive the money while he was too young to be able to take care of it. That is the reason the trust runs up to the time he is thirty years old.

Q. How was all of this going to protect your son?

A. Well, if I died and his mother died, he would have all this money, and when he was twenty-one years old it would be all his.

(Testimony of Edward D. Sultan.)

Q. Thirty years old, isn't it?

A. No, you asked me how it would protect without the instrument, I thought you meant.

Q. No, with the instrument. How would the trust protect [63] your son then?

A. Because when he is twenty-one years old he is only entitled to draw $300 a month.

Q. That is correct.

A. When he is twenty-five, I believes he receives $10,000. When he is thirty years old either there is some annuity clause in there or else the trust is terminated.

Q. If you decided to terminate the partnership, then what happened?

A. The money from the partnership goes into the trust and it carries on exactly the way I had planned it.

Q. But it would have to find itself another highly lucrative investment, wouldn't it?

A. Not necessarily. Certainly the profits of it were not invested in lucrative investments.

Q. There wouldn't be any profit.

Mr. Wild: I didn't understand that. You mean that they weren't invested in good investments?

The Witness: No, I misunderstood his question. I thought he was talking about if there was no partnership, and I was trying to show that even though there was money, it was invested in safe investments for the trust.

Q. (By Mr. Harless): Now at the time that the partnership was set up you have testified that there

(Testimony of Edward D. Sultan.)

was no discussion of any tax saving to you, is that correct? [64]

A. When the original discussions of the trust were had definitely there were no discussions of taxes. Taxes might have entered into it in some way.

Q. You think likely they came in somewhere along the line?

A. The form of which I don't remember. The taxes weren't a problem to us until 1942 when the business grew.

Q. You testified before, I believe, that at that point taxes weren't a very great problem. How much taxes did you pay on your 1941 and 1942 income?

A. I have to look at the tax returns.

Q. You don't remember?

A. No, I don't remember.

Q. Do you remember that when you sold the partnership your personal business that along with it went the liability for some $37,000 worth of your personal income tax for 1940 and 1941?

A. I didn't quite understand.

Q. Do you recall that when you sold the partnership your business that along with the assets and liabilities went a liability for your personal income tax for 1940 and 1941 in the sum of some $37,000, do you recall that, and the partnership paid it?

A. No, I don't recall it.

Q. You don't have any recollection?

A. I know that I left all my money in there,

(Testimony of Edward D. Sultan.)

and we paid [65] my taxes out of the business, out of my drawing account in the business.

Q. Those were your prior years' taxes?

A. Yes.

Q. In connection with the management of the business, when you were here in Honolulu, and perhaps even when you were elsewhere after the formation of the partnership, did you and Ernest discuss the business policies very extensively?

A. I always had.

Q. Did you discuss the business policies with your sister, Marie and your brother Gabriel?

A. Yes, we discussed them.

Q. Where?

A. In San Francisco.

Q. How often were you in San Francisco?

A. Three or four times a year, may have been more often. My brother was there many times.

Q. What was the extent of the discussions?

A. Well, probably to tell them what we had planned. They were very happy with their investment, and they didn't try to dictate.

Q. Did you and Ernest disagree on business policies after the formation of the trust at all?

A. I usually followed Ernest's dictates. I had a great deal of confidence in his managing ability.

Q. In the instances where you did not follow his dictates, what happened then?

A. I don't recall.

Q. Who prevailed?

(Testimony of Edward D. Sultan.)

A. I don't recall any such instances. We were very agreeable.

Q. You didn't find it necessary to take any vote among the general partners over a particular policy matter then in the business, is that correct?

A. No, we questioned them, I imagine, on policy. I can't think of any particular one that we questioned. Very few arose except the case of being able to buy merchandise for the islands.

Q. Was there any particular discussion about changes of salary for yourself and/or Ernest?

A. Yes.

Q. Was that ironed out?

A. Yes, that was discussed with Ernest, principally.

Q. Was it discussed at all with the other general partners?

A. Yes, and the Bishop Trust Company was informed of it, and they were agreeable to it.

Q. If they hadn't been agreeable, what then?

A. I don't know what we would have done, probably changed it.

Q. They really had no right to agree or disagree under the instrument, did they? [67]

A. They also were very happy with their investment and were very agreeable.

Q. To return for just a moment to the aid that you hoped this trust would give to your son, I should like to know why the instrument provides in effect that at age thirty your son shall receive the corpus and accumulated income of the trust and it shall

(Testimony of Edward D. Sultan.)

terminate, but if he should die sooner, then the proceeds go to his mother, your wife, and if she is no longer married to you, or if she has since deceased, it shall go to your sister Marie and your brother Gabriel and I believe your brother Ernest. Didn't you think that your son might get married at age twenty-one and have a family of his own that had to be provided for, or were you ignoring that possibility?

A. He had $300 a month. At the time we made up the trust there was very little money involved.

Q. And he was thirteen years old.

A. And he was thirteen, and he was a very brilliant boy, which he proved in high school, as graduating cum laude, and at thirteen he was on the school paper, and a boy that I had—not because he is my son—but I had a lot of confidence in him.

Q. Well, that's fine, but nevertheless isn't that provision, or wasn't that provision with respect to the trust income in the event of your son's death before thirty [68] designed to keep the interest in that business within your family?

A. No, sir. The sole reason in my mind was to not have him have a lot of money when he was too young to really have some experience in being able to handle it.

Q. He wouldn't have had a lot. Perhaps you misunderstand.

A. To me at the time when I made up the trust it was a lot of money. It was all I had.

Q. What I am getting at is this, in the event

(Testimony of Edward D. Sultan.)

that your son died before thirty, and I may say that the trust does terminate when he becomes thirty, isn't that correct?

A. Yes, I understand that.

Q. If he should die before that, then the trust income and the corpus goes to Mrs. Sultan, and under certain contingencies it might even go to your sister and brothers. Now didn't you anticipate that probably your son could have married and had a family and then died and still be before thirty? His death would leave his family practically destitute.

A. No, sir, it didn't enter into my mind at all.

Q. That was not anticipated? A. No.

Q. It was not a matter of trying to keep it in your family?

A. No, I don't remember it entering into the thing. [69]

Q. It just wasn't anticipated?

A. This is the first time I have given it any thought. There might be something there to handle it, but I can't recall right now.

Q. Who determined the amount of your salary?

A. My brother and myself discussed it. His salary was almost fixed, and it was determined between us and suggested to the trust company and our partners, who agreed to it.

Q. How long were you in the jewelry business, Mr. Sultan?

A. I started in when I was ten years old, and outside of a matter of six years, I have been in it all my life, or eight years.

(Testimony of Edward D. Sultan.)

Q. It is a rather complex business, isn't it?

A. Yes, it can be very complex, except that there are men in it that are successful that have been in for one or two or three years. It is a merchandising business.

Q. It is a merchandising, and it takes a salesman's touch or a merchandiser's touch and sense if you want to put it that way.

A. With a knowledge of the business, yes.

Q. You testified on direct that you had heard that another jewelry business here in town had a trust as a partner, and I believe you testified that you understood that was the Bishop Trust Company.

A. No, sir.

Q. Are you still under that understanding?

Mr. Wild: We object to that, if your Honor please, as a complete misstatement of the evidence. The evidence given on direct by this witness was that on the death that a trust company had taken over the management of one of his competitors and had finally pulled them out of a hole. They did it as the executor.

Q. (By Mr. Harless): What was the trust company that did that?

A. The Hawaiian Trust Company.

Q. When did your brother Ernest become ill in 1942? A. In the spring, I believe.

Q. And how long did that situation continue.

A. Several weeks.

Q. Several weeks only? A. Yes.

Q. A very short time?

(Testimony of Edward D. Sultan.)

A. No, to the extent that he had a very severe heart attack and almost died. He was in the care of two very prominent doctors here in Honolulu, Dr. Nils Larson, and Dr. Pinkerton, and when he straightened out he came back in the office, and that was the time we terminated his arrangement. He suggested he leave for the mainland, and I also felt that he should not have the responsibility of running the business. When he got up in the mainland, he felt better, within two or three or four months he felt that he would be able to handle the buying office in New York, which he did.

Q. And he went on to New York.

A. And at that time it developed that we needed such an organization.

Q. From the date of his recovery in 1942, did he remain in New York most of the time then, in the New York office?

A. Well, he had help in the New York office, and he made very frequent trips to Providence, Rhode Island, which is the jewelry manufacturing center, and to Los Angeles, where a lot of goods are bought, to San Francisco, where certain factory representatives were located, who we knew personally and who had been able to get us goods from responsible factories.

Q. But whose place of operation was Honolulu?

A. What?

Q. Who was in Honolulu? A. I was.

Q. Did you travel extensively too?

A. No, I made about one trip a year to the

(Testimony of Edward D. Sultan.)

States when I was able to get a priority to travel, and then helped with the buying, which was the important thing, and then came back here, and we had employed office managers all the time, some of them satisfactory and some of them not so satisfactory. [72]

Q. After the partnership articles were amended in 1942, that was about the time your brother recovered from his illness, what was the new arrangement as to his bonuses or salary?

A. I thought they were amended at his illness, not after.

Q. After, I said when he recovered?

A. They weren't amended after, to my knowledge.

Q. They were amended in June, 1942.

A. That was when he became ill.

Q. That is what I thought. Now, what was the arrangement?

A. At that time he was going to retire and take care of his health.

Q. And did he retire?

A. No. He did retire for a month or two and was under a doctor's care.

The Court: I think we have been into that, Mr. Harless.

Mr. Harless: That's right, your Honor.

Q. (By Mr. Harless): What was the salary arrangement he had then after he started to work the New York office?

(Testimony of Edward D. Sultan.)

A. When he started to work we were going back on the 25% again.

Q. And did you?

A. No, we decided on a bonus depending upon the year's profits. [73]

Q. What type of a bonus percentage?

A. So that he would draw practically the same as I did.

Q. Well, what per cent bonus was that of the year's profit?

A. I don't recall. It wasn't exactly a per cent; it was a flat figure.

Q. Do you remember what the flat figure was?

A. I have the figures.

Q. Well, I have the figures here, too, but it doesn't represent any percentage of an amount to be determined, does it?

A. No, it was determined when we saw how business was for the year.

Q. And who determined that, you and Ernest?

A. Ernest and I, with the consent of the partners.

Q. How was the consent of the partners obtained, by mail?

A. I was passing through San Francisco, and so was Ernest very often, and by mail also I imagine. We were in very close touch with our whole family.

Q. Now, with respect to the matter of your liquidating this partnership by offering to purchase the interests of the other persons, or the liquida-

(Testimony of Edward D. Sultan.)

tion of the partnership, it is stipulated, or there are exhibits attached to the stipulation which recite an offer on your part to purchase the 42% interest allegedly owned by the trust, and I believe you testified that you purchased the interests of your two [74] brothers and your sister as of January 31, 1949, is that correct?

A. Yes, sir, I think so.

Q. The purchase amount was the amount shown on the books as their capital investment plus their undistributed profits, is that correct?

A. That is my understanding.

Q. Where did the cash that was used come from?

A. From me, because the business owed me more than that, and Mrs. Sultan invested, I think, $60,000 of her own money.

Q. How much did you invest?

A. And I invested $60,000 more than I had, I think $127,500 against $46,000.

Q. And you actually had that cash?

A. And also the Bishop Trust Company, or my son rather, gave us $62,500.

Q. You actually had cash then to pay off the balances to your other partners?

A. Yes, sir. It might have been handled as a bookkeeping method. It might have been handled through my own account. I don't recall.

Q. Did all of the partners, both general and special, make additional capital contributions subsequent to 1941?

A. In the way of an agreement. I don't remem-

(Testimony of Edward D. Sultan.)

ber what year it was, but I think it was 1943 or 1944, where we needed capital in the business, and also wanted to as was explained. The Dunns, when I contacted them in San Francisco, advised me that the profits that were riding in our business and owed to the partners were considered a liability, and as they were almost up to what our net worth was in the business, we would have had a very bad financial rating, and it was talked over with the Bishop Trust Company and our accountant and my brother and everybody, and we finally contacted the Dunns, or they had told me in San Francisco that if that profit was tied up in the business, then the rating would change and we had a first-class rating, a fairly good rating, and that is what we did. We made an agreement to keep an equal amount as the original investment, making a total investment of $200,000 in the business. So they added $4,000 apiece.

Q. There was no cash contributed by anybody though, was there?

A. No, that was cash, undistributed profits.

Q. Isn't the net effect of that transaction that a book entry was made transferring amounts from advances due partners over into the capital account?

A. No, I don't know how that was handled.

Q. No cash came to you, did it? You just didn't withdraw a certain amount of your distribution for awhile?

A. The firm owed me the cash. I very seldom had any [76] cash except for my drawing account

(Testimony of Edward D. Sultan.)

of $2,000 a month or whatever I was drawing at different times, and that is the only cash I had on hand. The rest of it was left in the business to strengthen our business.

Q. In any event, this new capital contribution was not new money coming into your business, was it? A. Yes, it was.

Q. It was money made available through bookkeeping practices?

The Court: It depends upon the way you look at it. I think we have it clear. It was earnings left in undistributed.

The Witness: That's right.

Q. (By Mr. Harless): Now, in 1949 you testified that there was a radical change in business conditions due to a strike, is that right?

A. It was due to the strike and due to the fact that in 1948, I think it was 1948 in the fall, the services whom we had been selling large amounts had passed a ruling that they couldn't buy from Honolulu, and also our Guam business, which was very substantial, was almost entirely cut off, or 60% or 80% cut off, and the mainland wholesalers who compete with us here came down about that period and offered as long as I think eight and ten months terms to jewelers to buy volume, and in many cases we had to meet those terms. Yes. [77]

Q. Now, you testified I believe on direct examination that the business needed more money in 1949. A. The fall of 1948.

(Testimony of Edward D. Sultan.)

Q. And then you testified that you bought out the other partners.

A. The other partners' interest in the business was minor and they weren't interested in— They had seen me make an assignment in the jewelry business in 1932, and I had seen the whole house fall on me once before, and the Bishop Trust Company was very willing to sell out because the profits had dropped. The indications here were very bad, and the small amount that I bought out at $12,000 was of small consequence.

Q. The 42% was not of small consequence?

A. No, the 42 came back instead of $42,000 it came back in the business $67,500.

Q. It came in and out, or out and back in again?

A. Well, my son bought the interest in the partnership, and my wife put in sixty some odd thousand dollars.

Q. Your son had no cash to contribute of his own. He had to make a loan from the trust, is that right? A. Yes.

Q. Of which he was the beneficiary?

A. That's right.

Q. Did you indorse the notes which your son gave the trust [78] to secure the $62,000?

A. Yes, sir, and Mrs. Sultan indorsed them. The business guaranteed them. It is all in the papers there. I know that any bank would have loaned the money on the same, the most conservative bank in the world would have loaned that much money under the circumstances.

(Testimony of Edward D. Sultan.)

Q. That is your opinion, isn't it?

A. In my opinion, yes, sir.

Q. With respect to your relationship with the trust company particularly with the trust itself, did you often suggest investments or direct the trustee to make certain investments of the trust funds?

A. They were discussed with me and I suggested it, yes, sir.

Q. And where they would make such investments, you approved their actions, is that correct?

A. I approved anything, practically anything that they asked me to approve. I thought it was all right.

Q. And at least once didn't you instruct them to sell a considerable amount of securities contained in the trust?

A. My brother and I were in New York, and as I say, he was my financial advisor. He had played in the stock market at different times in his life and my experience there was practically nil, and I know that we wired them. I don't know whether it was our suggestion or what, that we would like to see them get out of the stock market. [79]

Q. And they got out immediately, didn't they?

A. I think so.

Q. You mentioned that you had had a number of discussions with Mr. White and Mr. Benner. Isn't it a fact that very many of those discussions had to do with the investment policies of the trust as distinguished from anything to do with the partnership?

(Testimony of Edward D. Sultan.)

A. It was with the partnership, practically—Even when my boy was eighteen years old he was in on some of the discussions as to investments, and so forth. He was consulted.

Mr. Harless: That's all, your Honor.

The Court: Any questions, Mr. Wild?

Mr. Wild: Yes, your Honor.

Redirect Examination

Q. (By Mr. Wild): Counsel just asked you a question about a wire which was signed, I think, by your brothers, Ernest and Edward, from New York, concerning recommendations of sale of all stocks. I will show you this wire and ask you if that is the communication to which he was referring?

A. Yes, sir, that was what I was referring to, and I imagine he was.

Q. Yes, and what is the Ernest whose name is signed on that? [80]

A. That is the co-partner.

Q. Is that also a co-trustee?

A. Yes, sir, co-trustee.

Q. Would you mind reading that wire into the record?

A. The date is April 27, received April 27, April 26 out of New York, received April 27, 1944.

The Court: Is that 1944?

The Witness: Yes.

The Court: I thought this inquiry was as to a later date.

(Testimony of Edward D. Sultan.)

The Witness: "Attention, W. A. White, Bishop Trust Company, Attention, W. A. White, Honolulu. We recommend you sell immediately all stocks Edward Sultan Jr. trust excepting government bonds including purchases spring 1942 and per your letter April 2 1943 and later Bulova stocks stop Also recommend investing entire proceeds in Series F war bonds stop Confirming letter in mail. Ernest and Edward Sultan."

Mr. Wild: No further redirect examination.

The Court: Step down, please.

(The witness was excused.)

Mr. Wild: Mr. Benner, will you please take the stand? [81]

EDWIN BENNER JR.

called as a witness in behalf of the Petitioners, being first duly sworn, was examined and testified as follows:

The Clerk: State your name and address, please.

The Witness: Edwin Benner, Jr., 4473 Aukai Street, Honolulu, T. H.

Mr. Wild: Counsel for the government is willing to stipulate for the purpose of saving time of Court and counsel that the first eleven questions and answers, including the Court's questions also beginning on page one to the top of page five in this transcript shall be considered as part of the record here.

The Court: What are those, pretty much qualifying questions?

(Testimony of Edwin Benner Jr.)

Mr. Harless: They are all qualifying questions. They run down to the very first question having to do with the partnership involved yesterday.

Mr. Wild: We so stipulate.

The Court: How is that going to be handled?

Mr. Wild: The reporter will be required to write it right in the transcript.

The Court: Very well.

(The portion of the transcript stipulated to above is quoted as follows):

Direct Examination [82]

Q. (By Mr. Wild): What is your present position, Mr. Benner?

A. I am Vice-president and Secretary of the Bishop Trust Company, Limited, and in charge of the trust department.

Q. How long have you been in charge of the trust department?

A. Since the spring of 1946.

Q. Prior to that time what was your position?

A. I was a trust officer of Bishop Trust Company.

Q. And for how long?

A. I joined the trust company in 1934, and I have been in the trust department at all times.

Q. I take it that your active business life, so far as your own participation is concerned since 1931 has been with Bishop Trust Company, Limited? A. That's right.

(Testimony of Edwin Benner Jr.)

Q. What was the Bishop Trust Company's capital in 1940 and 1941, if you recollect?

A. It was approximately $1,200,000 with a surplus of a like amount.

Q. And what type of business did it conduct at that time?

A. It conducted a trust company business here in the Territory. Banks do not do trust business and trust companies do not do banking business, and so during that entire time it was operated strictly as a professional fiduciary, with side issues such as insurance, real estate sales and brokerage, but its main business is administration of estates, trusts, [83] guardianships, agency accounts, acting as corporate trustee of all sorts and types, transfer agents, that type of business.

Q. In one fiduciary capacity or another do you have as part of your duties the management of various types of properties?

A. Yes indeed.

Q. You might explain that.

A. The normal trust or estate that we handle, of course, consists primarily of stocks and bonds or ownerships in real estate, but very often we have the problem of the administration of proprietorships or own the control or total outstanding shares of businesses, and these change year for year as the estates are probated and closed out. Some of our trusts have operated business for many years, though. I can give you a few examples.

Q. I wish you would give me some examples

(Testimony of Edwin Benner Jr.)
of businesses that you have operated in a fiduciary capacity.

A. We have just closed up an estate that has as its principal asset the controlling interest in a small structural steel company here in town with business operating right straight along. Our officer in charge was necessarily right on the job sometimes in the office, and so forth. We do own the controlling interest, through one of our fiduciary accounts, the largest specialty store, McInerny, Limited, that does $3,000,000 of business each year. I personally am secretary-treasurer of that company and sign all checks, incidentally. I receive daily statements of its sales volume by department all [84] the way through. We have a very active part.

Another business we are handling right now is the Honolulu Tile Business owned by the Worthington Estate. When Mr. Worthington passed away—it was his own business, and it was necessary that we step in and operate it, and not being familiar with that business we had some difficulty for several months and lost money until we were able to get things organized properly with an efficient manager, and are now pulling it out of the red and are doing very well. Our men in charge of that particular estate consult with me every week about their problems that they have there. They are on the job right along too.

We have handled dairies; we have handled ranches; we have handled ice cream business. In

(Testimony of Edwin Benner Jr.)

1944 and 1945 we administered the estate of Frances Wadsworth on the island of Maui. Mrs. Wadsworth at the time of her death was owner of the Maui Soda and Ice Works. That business owned the Coca-Cola franchise on the island of Maui. I made 18 trips to Maui during the year 1945 in connection with that business, taking a very active part in it.

The Court: Is that as executor?

The Witness: We were temporary administrators to start with, the license was issued in our name at first, and then to us as executor.

The Court: And what do you do there, try to liquidate the company as quickly as possible? [85]

The Witness: We operated it just about a year. In 1944 and 1945 were boom years here in the islands because of the tremendous number of service people here, and bottling companies and business of that nature did a tremendous business, and rather than a liquidation program we continued to operate so that we would have a going business to sell to someone. We negotiated a sale eventually to a man who had been the West Coast agent for Coca-Cola. He was able to secure the consent of the Coca-Cola Company.

Mr. Nyquist: Objection, your Honor. I don't think there is any occasion to go into other bottling company cases.

The Court: We don't need to go any further on that.

Q. (By Mr. Wild): What other type of business?

(Testimony of Edwin Benner Jr.)

A. I just jotted down a few, auto sales——

The Court: I think that is enough.

The Witness: We have the Ford agency in Hilo right now that we are administrating.

(End of stipulated portion of transcript.)

Q. (By Mr. Wild): Mr. Benner, will you kindly state what your connections were with the Edward Sultan Trust?

A. Well, as a trust officer of Bishop Trust Company in 1941 and 1942, I became acquainted with the Edward Sultan trust. The trust itself was administered primarily by Mr. W. A. White of our office, and I worked with him on his accounts as he did with me on mine. [86]

Q. Yes.

A. When he was away from the office, I took care of his affairs, and even sat in with him on discussions that he had with many trusts, and this trust also.

Q. I see. Now, as a part of your duties and responsibilities there at the trust company, did you discuss the method of having an inter vivos trust a partner in a going business?

A. Yes, I remember the discussions.

Q. Do you remember what occurred here in this case? A. Yes, I do.

Q. Can you state briefly what it was and what the purpose of it was?

A. Well, we were approached, I believe it was Mr. Cades who approached us, to see if we would be willing to act as co-trustee of this Edward Sultan

(Testimony of Edwin Benner Jr.)

Trust. The principal asset of the trust would be an interest in a partnership. This is the first case that we had ever had, or it would be the first case we had ever had where we were to act in that capacity in an inter vivos trust. We were a little uncertain as to whether or not under the Territorial statutes we should recognize it as a proper trust investment. It was new to us. We indicated, however, after some discussion there in the office, that we would be willing to act provided the proper court here in the Circuit Court in equity approved of such an investment, and so indicated to [87] Mr. Cades. The proper petition was entered and a hearing was held. I did not attend the hearing. An order was entered.

Mr. Wild: The petition and decree are in the record as stipulated, your Honor.

Q. (By Mr. Wild): Mr. Benner, what was your own connection with following the business of the partnership, the special partnership of Edward D. Sultan Company?

A. My contact was only intermittent, as Mr. White was very often there, and our joint discussions when I was present and when I talked with Mr. Sultan alone were primarily concerned with how business was going, his difficulty due to the war here of getting shipments out here and the growth of the business itself, and I think he was somewhat irritated on our continued insistence to withdraw our share of the profits. We thought that we should have them out as soon as they could be withdrawn. The statements indicated large cash balances were

(Testimony of Edwin Benner Jr.)

maintained, and as it took several mouths generally to prepare the statements, we thought that by that time enough funds should be available to carry on the business if they paid us out our share.

Q. Mr. Benner, what were the assets of the trust known as the Edward D. Sultan trust in August, 1943?

A. Would it be permitted that I refresh my memory on that?

Mr. Wild: That was the date that your Honor asked about, asked the other witness, if my recollection is right. [88]

The Court: I don't remember what was the significance of that.

Mr. Wild: Just what the assets were in the trust just before the tax years involved.

The Witness: The assets were the 42% interest in the partnership known as the Edward D. Sultan Company, and common stocks, some Series F. bonds, and cash totaling $140,000. This represented distributed and the investment income. In other words, we had $180,000 assets in the trust as of that date.

Q. (By Mr. Wild): So that the $40,000 is a little less than—it is a small fraction of the total assets of the trust at that time? A. Yes.

The Court: Well, that is of course, I suppose, based on cost.

The Witness: Yes, sir.

The Court: And it might very well be that the interest in a partnership with these huge earnings

(Testimony of Edwin Benner Jr.)

would be much more than that. In other words, that 42% worth——

The Witness: $42,000.

The Court: Your annual earnings were far above that weren't they?

The Witness: That's right. This is book value.

Q. (By Mr. Wild): And the other securities there are at [89] book value?

A. That's right.

Q. Not market value at that time?

A. That's right.

Q. Now Mr. Benner, at the time of the negotiations leading up to the sale of the interest in the partnership by the trust, did you participate in those?

A. Yes, I was the officer in charge of the account at that time.

Q. All right, will you recount what happened?

A. The first thing that happened was the receipt of a letter, an offer from Mr. Sultan, and a discussion then followed as to whether—the discussion incidentally was in our office—as to whether, Mr. Sultan felt that he could only continue with a larger capital, we should indicate to him that we would prefer that the partnership interest not be sold and that we contribute more capital. We knew we were already in the business. We decided against making that suggestion. We felt that the business had grown enormously during the war years and was stabilized off and might decrease, and we felt that we had enjoyed very good earnings. We had

(Testimony of Edwin Benner Jr.)

drawn them out. We had invested them and we were holding them for our beneficiary, and that it would be to the best interest of the trust to sell this interest to Mr. Sultan, and we so informed him by letter about a week [90] or ten days later.

Q. And after that decision was made did the other trustee participate in it, approve it?

A. He approved of it, yes.

Q. And what was done then?

A. Well, this proposal was made in February and was to take effect as of the end of January, 1949, and it took some little time to complete their January 31, 1949 auditing statement which was to determine exactly what was their distributive share of the income. When those reports were prepared Mr. Sultan submitted the reports to us, and at the same time a statement of our share according to these reports, our share of the accrued income, our credit on their books, I think it was called. He submitted this check on the 27th of April. A few days prior to that a loan had been negotiated with us from this same trust for $62,500. The loan was to be made to Edward D. Sultan, Jr., the beneficiary and remainder man. The request for the loan was discussed in our office and was referred to counsel for advice as to whether it would be permitted under the terms of the trust. We were advised by letter that it was, provided we felt it was a proper business risk. As I recall, this letter also suggested that as to the security that we should request, which was the assignment from young Mr. Sultan of his

(Testimony of Edwin Benner Jr.)

monthly payments due him from the trust as [91] they were due, his remainder interest in the trust, and indorsements by his father and mother. This was considered by us in the trust company. We felt that it was a good business risk for this trust. There was ample security for the loan.

Q. What about the interest that young Mr. Sultan was to receive in the proposed new partnership? Was that to be hypothecated also?

A. I forgot to mention that. It was also. In other words, we had hypothecated his interest in the partnership and the indorsement of the other partners, besides the trust itself which was worth something over $200,000.

Q. Has it been unusual in past years for trustees to make loans to beneficiaries of a trust?

A. We do it in some cases. We don't make a general practice, our difficulty being, very frankly, the difficulty in dunning the beneficiary for interest payments and their inability to pay, but we did not have that situation here. We had an automatic assignment of payments that were to be distributed to him from the same trust which would merely be journalized over on our books and would never get into his actual possession, as a matter of fact. When they were due every month, they were merely journalized.

Q. What has happened to this note?

A. It has been paid down according to the terms of it. All [92] payments have been met.

Mr. Wild: No further direct.

(Testimony of Edwin Benner Jr.)

Cross-Examination

Q. (By Mr. Harless): Mr. Benner, were you connected with this particular trust at the time it was created?

A. I was the co-signer with Mr. White as trust officers in the Bishop Trust Company. I believe I met Mr. Sultan then. I am not certain. I met him along about that same time because it is our practice to have officers who handle the accounts to meet the clients as soon as possible.

Q. Now in connection with the services rendered by the trust as a special partner to the partnership, were there very many discussions between the trust company and either Mr. Ernest Sultan or Mr. Edward Sultan relative to the business policies and the method of operation of the partnership?

A. Well, as to Mr. Ernest Sultan, I never met him. He was here only a short time after the trust was created, and I never have met him at all. He has never been back here, as far as I know, since he left in June, 1942. Our correspondence with him has been more relative to the general investments of the trust other than the partnership, it being my information direct from Mr. Sultan that he talked with his brother. Now he, I think he testified himself [93] a few moments ago—Our contacts with Mr. Sultan, and that goes for myself and my observation of Mr. White in his contacts, occurred periodically, maybe three or four or five times a year, Mr. Harless, probably not more often than that, and concerned, as I said a while ago, of how business

(Testimony of Edwin Benner Jr.)

was going. I was aware myself when he said that they had opened a New York office, and we thought that under the circumstances to expedite the buying that it was a very good idea and thoroughly approved of what they were doing.

Q. Well, when various and sundry policies were adopted, was the trust company advised or informed, or were you invited to participate in the discussions?

A. Well, I could answer that yes and no, because on some occassions it was a discussion of what he would like, but other times it was, "We have done this, and I hope it is all right".

Q. Isn't it a fact that many of the discussions and much of the correspondence with Mr. Edward Sultan also had to do with the trust and the investments that might be made by the trust as distinguished from the partnership problems?

A. Originally yes, but during the last several years our investments have been fairly well fixed in bonds, and we haven't had occasion to have that contact for that purpose.

Q. As a matter of fact, isn't it true that all of the investments since the date in April, 1944, in which certain [94] stocks were sold as a result of the radiogram read into the record have been government bonds of one sort and another?

A. With one exception.

Mr. Wild: We object to that. It assumes a lot of things which are not in evidence. It says these bonds were sold as a result of the radiogram read

(Testimony of Edwin Benner Jr.)

in the record. It implies that the trust company had no activity in it. We merely read the radiogram which counsel had brought out.

Q. (By Mr. Harless): Do you have your file with you, Mr. Benner? A. Yes, I have.

The Court: I don't know whether—is this of any particular consequence?

Mr. Harless: Not particularly. I will withdraw the question.

Q. (By Mr. Harless): Mr. Benner, did the trust company sell those stocks as a result of that radiogram? A. Yes, we did.

Q. Immediately? A. Yes.

Q. Did you consider that to be a direction on the part of Mr. Edward, Mr. Ernest Sultan, the trustee?

A. No, not a direction. It was a recommendation and so stated in the wire.

Q. And you accepted it as such? [95]

A. Yes, we did. It came from our co-trustee as well as the settlor.

Q. What type of investment has the trust put the money in since that date?

A. We now have it invested in bonds and a note.

Q. And the note? A. Yes.

Q. You testified somewhat about your continued insistence on payments from the partnership over to the trust. A. Yes.

Q. Were there a number of times that you found it necessary to either telephone or write asking for funds to be distributed?

(Testimony of Edwin Benner Jr.)

A. Well, we use a tickler system there so we won't overlook these things, and they automatically come up, and if the report hadn't come in, Mr. White's secretary would write a letter and if he was available he would sign it. If he was not available I would sign it, just to get it in the record that we wanted to get his report in and his payment.

Q. You needed money or a report?

A. Under our distributive share. They were generally very prompt.

Q. Now isn't it true that there were occasions when your correspondence became somewhat insistent because tax payments were coming due and there was not sufficient cash in the trust? [96]

A. That's right. We had income invested and we preferred not to sell any of the bonds as long as we knew we had the credit with the partnership, and in reviewing the file myself I ran across an occasion where we had, in December of one year, apparently advanced the December 15 payment, and we were OD on our books, and Mr. Sultan was back in New York, and he directed that payment be made and it came over immediately.

Q. By OD you mean the trust was overdrawn?

A. Yes, overdrawn on our books, which is a situation we do not ordinarily permit.

Q. In connection with this matter of distribution under the trust instrument and under the partnership instrument, did the special partner have the power to force a distribution?

A. No, we had to ask him for it.

(Testimony of Edwin Benner Jr.)

The Court: The provisions in the agreement state what can be done.

Mr. Harless: That's right, your Honor.

The Court: I don't think we are adding to it by just asking the same thing again.

Q. (By Mr. Harless): Were you ever in the offices of the Sultan Company, Mr. Benner?

A. Yes.

Q. You had occasion to go over there?

A. Yes. [97]

Q. On business in connection with the partnership?

A. Yes, not many times, just two or three times, but I have been there.

Q. As an ordinary matter, would an interest in a partnership business be the type of investment that your company would make?

A. It was so unusual that we went into court to have it approved by the court before we would accept this. Subsequently we have had quite a number of partnership interests in trusts.

Q. This same arrangement, a similar arrangement? A. In a general way.

The Court: That is where the initial corpus is of that character?

The Witness: Yes, sir.

Q. (By Mr. Harless): In that connection, why wouldn't a partnership interest ordinarily be a good trust investment from your experience as a trust officer? Is the risk too great?

A. Well, there is too much liability attached to

(Testimony of Edwin Benner Jr.)

an investment like that. In this instrument I think you will find that there is a release of any liability from this investment, and our normal policy is to go into a more conservative diversified schedule of investments of stocks and bonds, preferred stocks and real estate, and so forth, [98] not this, it is too volatile.

Q. Is it your company's policy to insist upon a release of liability in a normal situation where you are going into good stocks and bonds?

A. If it is an inter vivos trust we ask that as a standard provision from any attorney that prepares any document that we are going to ask.

Q. Isn't it a fact that the trust company as trustee might not have been interested in acting in this case if the business wasn't being managed by Mr. Ernest and Mr. Edward Sultan? In other words, didn't you look to their management as one of the major assets of the business?

A. You mean if the settlor himself had not been interested in it?

Q. That's right.

A. I believe we would have insisted on satisfying ourselves that there was competent management in it, because we recognize that in this particular case there might be a time when we might have to take over and do with what management might be left there, and to eventually find an adequate management.

Q. Did you participate in any of the discussions

(Testimony of Edwin Benner Jr.)
that preceded the establishment of both the trust and the partnership?

A. No, sir.

Q. Who in your firm did participate in those discussions? [99]

A. My first knowledge of it came from Mr. White. He told me that he had talked with Mr. Cades, and he discussed with me as to whether it would be something that we should go into or not.

Q. When was your first contact with this trust and partnership after it was formed or just before?

A. I signed the document. That was my first contact. I had discussed it beforehand with Mr. White.

Q. But not with Mr. Sultan?

A. No.

Q. Nor Mr. Cades?

A. No, I did not talk with Mr. Cades.

Q. Now you testified on direct concerning some discussions held within the trust company in 1949 after you had received a letter from Mr. Edward Sultan relative to an offer to purchase the 42% interest, and I believe you testified that at that time you even considered trying to stay in the business, is that right? A. Yes.

Q. Make a further capital contribution?

A. That was part of the discussion as to the advisability.

Q. The trust had already made something of a capital contribution in 1944 or 1945, had it not?

A. Well, that was just a temporary situation during a boom period in order to improve the credit

(Testimony of Edwin Benner Jr.)

rating of this partnership. [100] That's all it was. It was only for a limited time. It was not adding capital for a permanent proposition. We got it back when we were supposed to get it back.

Q. You got it back?

A. Yes. There was a tremendous change between 1944 and 1949 in our economic condition here in the islands.

Q. Did the trust company think that the continued participation in this partnership was a good investment in 1949?

A. From my discussion with Mr. Sultan when this letter came in, it was obvious that he had to have more capital. There was no question about that. I was well satisfied, and he had a good proposition to buy us out. Incidentally, I think he stated—it shows in the letter—a purpose that he had always had in mind, that his son would actually himself personally buy into this partnership as soon as it could be arranged.

Q. Well, then, he wasn't interested in bringing you into it, the trust company or the trust into the partnership on a greater scale?

A. He did not make that suggestion, but it was our duty as a trustee to study it from all angles. We weren't going to simply do what Mr. Sultan proposed, not at all. We had to reason it out ourselves.

Q. You decided not to go in? [101]

A. That's right.

Mr. Harless: That's all.

Mr. Wild: No redirect, your Honor. The Pe-

titioners rest, subject to having those exhibits furnished.

Mr. Harless: The Respondent has no further matter except the exhibits.

[Endorsed]: T.C.U.S. Filed July 18, 1951.

* * * * * [102]

[Endorsed]: No. 13804. United States Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. Edward D. Sultan, Respondent. Commissioner of Internal Revenue, Petioner, vs. Olga L. Sultan, Respondent. Transcript of the Record. Petitions to Review Decisions of the Tax Court of the United States.

Filed April 13, 1953.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 13,804

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

EDWARD D. SULTAN and OLGA L. SULTAN,
Respondents.

PETITIONER'S DESIGNATION OF RECORD ON APPEAL

The petitioner hereby designates for inclusion in the printed record on appeal the following portions of the typewritten record received by this Court from the Clerk of the Tax Court of the United States in the above-entitled cause:

1. Docket entries, No. 24,513.
2. Docket Entries, No. 24,514.
3. Petition (with exhibit), No. 24,513.
4. Answer, No. 24,513.
5. Amended answer, No. 24,513.
6. Petition (with exhibit), No. 24,514.
7. Answer, No. 24,514.
8. Amended answer, No. 24,514.
9. Stipulation of Facts, with Exhibits 1 through 14, 23 through 26.
10. Transcript of Proceedings, 6-19-51, pp. 1; 23 through first six lines on p. 102.
11. Findings of Fact and Opinion.
12. Decision, No. 24,513.

13. Decision, No. 24,514.
14. Petition for Review, No. 24,513.
15. Petition for Review, No. 24,514.
16. Statement of Points, No. 24,513.
17. Statement of Points, No. 24,514.
18. This Designation.

Dated: April 28, 1953.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
Attorney for Petitioner.

[Endorsed]: Filed Apr. 30, 1953. Paul P. O'Brien, Clerk.

No. 13,804

In the United States Court of Appeals for the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE, PETITIONER,

v.

EDWARD D. SULTAN, RESPONDENT.

COMMISSIONER OF INTERNAL REVENUE, PETITIONER,

v.

OLGA L. SULTAN, RESPONDENT.

ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE PETITIONER

H. BRIAN HOLLAND,
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Special Assistants to the Attorney General.

AUG 24 1950

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ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE PETITIONER

OPINION BELOW

The opinion of the Tax Court (R. 159-178) is reported at 18 T. C. 715.

JURISDICTION

The petitions for review in these cases involves deficiencies aggregating $406,452.34 in the federal income taxes of the taxpayer Edward D. Sultan and his wife [1]

[1] The taxpayer's wife is involved only because of the community property law of Hawaii which became effective on June 1, 1945. (R. 160.)

for the years 1944 through 1946. (R. 5, 26, 179-191.) On April 26, 1949,[2] the Commissioner of Internal Revenue mailed to the taxpayer and his wife notices of deficiencies in their income taxes for the years in question. (R. 14, 34.) Within 150 days thereafter, on August 12, 1949, the taxpayer and his wife, pursuant to Section 272 of the Internal Revenue Code, filed petitions with the Tax Court for redetermination of such deficiencies. (R. 4-24, 26-37.) The proceedings were consolidated for hearing in the court below. (R. 2, 4.) On October 31, 1952, decisions of the Tax Court were entered redetermining the deficiencies. (R. 179, 180.) On January 10 and 19, 1953, the Commissioner filed his petitions for review invoking the jurisdiction of this Court under Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948. (R.181-187.)

QUESTIONS PRESENTED

1. Whether in transferring property in trust for the benefit of his minor son the taxpayer retained sufficient control over that property to be treated for tax purposes as the recipient of income therefrom when (a) the trust was required to use that property to purchase a special or limited partner's interest in a simultaneously created family partnership in which the taxpayer was the controlling general partner, and (b) the trust was not free to terminate or transfer its interest once the partnership was created.

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[2] There were added to the gross income of the taxpayer and his wife for each of the years in question amounts in excess of 25 per cent of the gross income stated in their returns. (R. 16, 19, 22, 35.) Accordingly, under Section 275(c), Internal Revenue Code, assessment and collection of the deficiencies were not barred by the statute of limitations.

2. Whether a trust, which the taxpayer claims should be recognized for tax purposes as a special or limited partner solely on the basis of its contribution of gift capital to the partnership, was the true owner-contributor of such capital when it was not free to withhold such capital from the partnership, to transfer the partnership interest allegedly acquired for that capital, or to withdraw from the partnership either the capital or income attributable to it.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and Regulations are set forth in the Appendix, *infra*.

STATEMENT

The facts found by the Tax Court, which are based in part upon a stipulation (R. 43-158) may be summarized as follows:

The taxpayer, Edward D. Sultan, and his wife, Olga, were residents of the Territory of Hawaii. They had one child, Edward D. Sultan, Jr. born December 28, 1927. (R. 160.)

The taxpayer had been in the wholesale jewelry or jewelry manufacturing business since he was about 10 years old. In the early part of 1941, he was in the wholesale jewelry business as an individual in Honolulu. That business consisted of dealing in watches, diamonds, silverware, general jewelry lines, and everything associated with a jewelry business (R. 160.) The taxpayer was primarily a salesman. The manager of the business was his brother, Ernest W. Sultan, who received as compensation 25 per cent of the net profits of the business. The taxpayer devoted most of his time to selling in the Far East and in the Pacific Islands. Ernest had no

financial interest in the business but was very valuable to it because of his knowledge of the jewelry business. (R. 160-161.)

For some time prior to August 1941, the taxpayer had been considering ways and means of protecting his family in the event of his illness or death, and also of interesting his son in the business. The son, who was 13 years old in 1941, was interested in the study of journalism and not in the jewelry business. The taxpayer at that time was almost constantly in the care of doctors. In 1940, while the taxpayer was on a trip, his brother Ernest became seriously ill and was away from the office for a few weeks. (R. 161.)

Another brother of the taxpayer, Gabriel, was a full time salesman of the taxpayer's merchandise in California. The taxpayer's sister, Marie Hilda Cohen, was in San Francisco, where she and her husband owned a warehouse and they frequently supplied warehouse space for the taxpayer's merchandise while it was awaiting shipment to Honolulu. In the early part of 1941, it was difficult to obtain shipping space. The taxpayer's sister was a capable business woman. (R. 161.)

The taxpayer discussed with his brothers and sister possible methods of having his business carried on for the protection of his wife and son and of interesting his son in the business. He also discussed the matter with his wife, with a relative in the United States who was a lawyer, and with counsel in Honolulu. Out of these discussions there was evolved the idea of the creation of a trust and the formation of a partnership. The taxpayer knew of one instance in which a jewelry business which was in bad financial shape had been rehabilitated under the management of a trust company. He wanted

a trust company as trustee of the trust to be created for his son for the benefit of the advice which it could give and for the management which it could provide in the event he was not able to carry on the business. He wanted his brothers and sister associated with him in the business for the assistance they could give as they had in the past. (R. 161-162.)

The Bishop Trust Company, an Hawaiian corporation, conducted a trust company business in the Territory of Hawaii. Its main business was the administration of estates, trusts, guardianships, agency accounts, and it acted as transfer agent, and did similar business. In its fiduciary capacity, it often operated businesses in connection with its administration of estates or trusts. (R. 162.)

On August 28, 1941, the taxpayer created the Edward D. Sultan Trust, naming as trustees Ernest W. Sultan and Bishop Trust Company. The trust instrument recited the delivery to the trustees of the sum of $42,000 by the settlor, to be used to purchase a 42 per cent interest in a partnership known as Edward D. Sultan Company. Income was to be accumulated until the settlor's son became 21 years of age, but with discretion in the trustees to pay out not more than $3,600 per year for the maintenance, support and education of the beneficiary. Beginning at the age of 21, the beneficiary was to receive $300 per month; at the age of 25 he was to receive a portion of the accumulated income in a lump sum. At the beneficiary's age of 30 years, the trust was to terminate and he was to receive the trust corpus, together with any cash in the estate not in excess of $20,000. Any remaining cash was to be used to purchase an annuity for the beneficiary. If the beneficiary

died before the age of 30, corpus and income were to go to the wife of the settler, or, in the event of the happening of specified events, to the settlor's sister and brothers. (R. 162-163.)

The trust instrument gave the trustees the usual powers to hold and manage the trust property, collect the income, and invest and reinvest. The trustees were not restricted to investments of the type which are permitted by law, with the provisos that during the lifetime of the settlor the trustees were to obtain the settlor's consent to investments, and upon the settlor's death they were to be restricted to legal trust investments. However, the trustees could in any event make loans or advances to the partnership without liability for resulting losses. The trust was irrevocable. The corporate trustee was given custody of all money and securities in the trust estate. The settlor reserved the right to transfer additional property to the trust. Under the terms of the trust instrument neither the corpus nor income of the trust was ever to be paid to the settlor. The trust was conditioned upon obtaining court approval for the purchase of a 42 per cent interest in Edward D. Sultan Company, and approval of the trustees becoming a special partner therein. If such approval was not obtained within 60 days, the trust indenture was to be null and void. (R. 163-164.)

On August 30, 1941, a partnership was formed under the name of Edward D. Sultan Company. It was a special partnership. The general partners were the taxpayer, Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan. The trustees of the Edward D. Sultan Trust were a special partner. The initial capital of the partnership was $100,000. (R. 164.) Contributions of

capital and partnership interests were as follows (R. 164):

Partner	Contribution	Interest
Edward D. Sultan	$46,000	46%
Ernest W. Sultan	4,000	4%
Marie Hilda Cohen	4,000	4%
Gabriel L. Sultan	4,000	4%
Trustees of Edward D. Sultan Trust	42,000	42%

The partnership was to acquire the assets and carry on the business theretofore conducted by Edward D. Sultan. The general partners actively engaged in the business were to receive compensation for services rendered in such amounts as the general partners might agree on, and such compensation was to be charged as an expense in computing net profits. As long as Ernest W. Sultan was active in the business, he was to receive 25 per cent of the net profits. The remainder of the profits was to be divided in proportion to the capital contributions of the partners. The provision for Ernest W. Sultan to receive 25 per cent of the net profits was stricken from the agreement by amendment dated June 9, 1942. Profits could be withdrawn at such time as the general partners deemed advisable. (R. 164-165.)

Only the general partners had authority to transact partnership business and incur obligations. The policy of the partnership was to be established by the general partner or partners owning the majority in interest of the capital. No general partner could assign or mortgage his or her interest, but any partner could purchase the interest of any other partner. The special partner could assign its interest with the consent of the general partners. (R. 165.)

Proper partnership books of account were to be kept. The books were to be audited periodically and copies of auditors' reports were to be furnished to each partner. Annual accounts were to be taken showing the interest of each partner and copies thereof were to be sent to each. (R. 165.)

The partnership could be terminated by a majority in interest of the general partners on two months' written notice. The taxpayer had the option to purchase the interest of any deceased general partner or of any partner who gave notice of termination. Such purchase was to be the book value without allowance for good will. (R. 165.)

Originally the partnership was to continue until April 30, 1943, and thereafter from year to year until terminated by a general partner on six months' notice. By amendment dated February 2, 1945, the term was extended to January 31, 1946, and thereafter from year to year. (R. 165.)

By bill of sale dated as of the close of business on August 30, 1941, the taxpayer transferred to the partnership all of the rights, property, assets, privileges, and business formerly carried on by him, having a stated value of $100,000. He received back demand notes made by him on August 28, 1941, payable to the trustees of Edward D. Sultan Trust in the amount of $42,000 and to Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sultan, each in the amount of $4,000. He also received a 46 per cent interest in the partnership. (R. 165-166.)

The required certificate of partnership and affidavits were filed and publication was duly made. (R. 166.)

On September 5, 1941, the trustees of the Edward D. Sultan Trust filed in the First Circuit Court of the

Territory of Hawaii a petition to become a special partner in Edward D. Sultan Company and to invest $42,000 in the partnership for a 42 per cent interest therein. On September 9, 1941, the court entered an order in which it instructed, authorized, and directed the trustees to become a special partner in the partnership and to invest $42,000 therein. (R. 166.)

On or before March 15, 1942, the taxpayer filed a gift tax return for the year 1941 in which he reported a gift of $42,000 to the Edward D. Sultan Trust. The Commissioner determined that the value of the 42 per cent interest in the partnership was greater than the reported amount of $42,000 and that additional gift tax was due in the amount of $81.99 which amount the taxpayer paid. (R. 166.)

Ernest W. Sultan managed the partnership business until he became ill in 1942 and was required to leave the islands. The taxpayer at that time took over the management. Ernest recovered quickly and, at the request of the taxpayer, opened a buying office in New York for the partnership and continued in the service of the partnership as a buyer. (R. 166-167.)

The corporate trustee was given annual auditor's statements of the partnership business, and the taxpayer gave it oral interim statements. The taxpayer discussed business policies with officers of the corporate trustee, and conferred frequently with the other trustee on partnership matters. (R. 167.)

The partnership made it a regular practice to pay for merchandise on the day of receipt of the invoice even though delivery to it was delayed, sometimes for months, due to the demand for shipping space and restrictions on shipment by parcel post. This practice, and an expansion of the business following the outbreak

of World War II, brought about a need for more capital in the business. In order to provide the needed capital and to improve the partnership's credit rating, the partners agreed in 1942 or 1943 to leave earnings in the amount of $100,000 in the business to be used as working capital. This matter was discussed with officers of the corporate trustee. (R. 167.)

The taxpayer and his brother Ernest W. Sultan received compensation for services rendered to the partnership for the periods and in the amounts as follows (R. 167-168):

	Edward D. Sultan	Ernest W. Sultan
Sept. 1, 1941 to Jan. 31, 1942	$ 6,500.00	$23,000.00
Feb. 1, 1942 to Jan. 31, 1943	20,431.13	95,169.99
Feb. 1, 1943 to Jan. 31, 1944	42,000.00	60,000.00
Feb. 1, 1944 to Jan. 31, 1945	42,000.00	60,000.00
Feb. 1, 1945 to Jan. 31, 1946	42,000.00	50,000.00
Feb. 1, 1946 to Jan. 31, 1947	64,000.00	15,000.00

During the existence of the special partnership, the trustee was quite insistent on having the special partner's distributive share of profits paid over to it as soon as possible after financial statements were prepared. Payments of the trust's distributive share of the partnership profits were made to the corporate trustee as follows (R. 168-169):

Payments made		Payments made	
June 23, 1942	$ 24,754.29	March 12, 1945	$83,029.40
March 15, 1943	2,000.00	March 17, 1945	50,000.00
March 23, 1943	108,913.64	March 21, 1945	25,000.00
October 8, 1943	2,198.94	April 6, 1946	42,000.00
March 15, 1944	16,640.00	May 21, 1946	99,698.24
June 14, 1944	19,000.00	January 14, 1949	2,155.75
September 2, 1944	21,000.00	March 14, 1949	10,000.00
September 21, 1944	97,457.03	April 28, 1949	85,357.62

In 1948, the partnership business fell off, due partly to increased competition. In January, 1949 the taxpayer purchased the interests of the three other general

partners, namely, Ernest W. Sultan, Marie Hilda Cohen, and Gabriel L. Sulton. A formal bill of sale was executed wherein the three selling partners agreed to the termination of their interests in the partnership. (R. 169.)

In February, 1949, the taxpayer offered to purchase, and the trustees of the Edward D. Sultan Trust agreed to sell, the trust's interest in the partnership. The price agreed upon, in an exchange of letters, was a sum equivalent to the capital investment in the partnership, plus the amount of the unpaid profits accumulated to January 31, 1949. At that time, the beneficiary of the trust, Edward D. Sultan, Jr., had attained his majority, and had been active in the partnership business during his summer vacations from college. (R. 169.)

The officers of the corporate trustees gave thorough consideration to the taxpayer's offer before accepting it. They were aware of the need for additional capital in the business and of the possible decrease in the business of the partnership. They decided that it would be to the best interest of the trust to sell its share of the partnership to the taxpayer. The cotrustee, Ernest W. Sultan, approved the sale. (R. 169.)

The agreement was carried out through the medium of a bill of sale whereby the taxpayer and the trustees of the Edward D. Sultan Trust, as the "seller", sold the assets and business of the partnership to a new partnership known as Edward D. Sultan Company, in which the partners were the taxpayer, his wife Olga, and Edward D. Sultan, Jr. (R. 169-170.)

The new partnership started with a capital of $250,000. Of this amount, the taxpayer contributed $127,500, the taxpayer's wife contributed $60,000 from her own funds, and Edward D. Sultan, Jr., contributed $62,500.

The son, Edward D. Sultan, Jr., obtained the amount of his contribution by way of a loan made to him by the Bishop Trust Company, from the corpus of the Edward D. Sultan Trust. The money was loaned on the note of the son, which note was endorsed by both the taxpayer and his wife. As additional security for the loan, Edward D. Sultan, Jr., assigned to the trust company his remainder interest in the trust and his right to monthly payments of $300 which began when he reached the age of 21 years. The taxpayer never received from the trust any of its income. During the years involved in these proceedings, the taxpayer Edward D. Sultan supported his wife and son from his own income. (R. 170.)

At August 28, 1950, the end of the last fiscal year of the trust prior to the hearing in these proceedings, the trustees of the Edward D. Sultan Trust held intact the corpus of the trust estate, which consisted of the following items: cash, $9,842.58; United States Government Bonds, $171,872.61; note receivable of Edward D. Sultan, Jr., $60,782.14, the total of which amounted to $242,497.33. (R. 170-171.)

The Edward D. Sultan Trust duly filed fiduciary tax returns each year and paid the tax shown to be due thereon. The partnership, Edward D. Sultan Company, filed its partnership tax returns on an accrual and fiscal year basis ending on the 31st day of January. Its first return was filed on that basis for the fiscal year ended January 31, 1942. Returns on that basis were filed for subsequent years ending January 31, 1943 to 1949, inclusive. (R. 171.)

By virtue of the Hawaii community property law, which became effective as of June 1, 1945, the taxpayer's wife Olga was entitled to one-half of all of the income

of her husband, the taxpayer, from and after that date. The entire deficiency proposed against her arose by reason of her community property interest in the income of her husband. (R. 171.)

The Edward D. Sultan Trust was a bona fide trust created for the benefit of Edward D. Sultan, Jr., and the taxpayer and his wife did not have any substantial control over, or interest in, the corpus or income thereof. (R. 171.)

The taxpayer, Ernest W. Sultan, Marie Hilda Cohen, Gabriel L. Sultan, and the Edward D. Sultan Trust really and truly intended to join together for the purpose of carrying on the business of Edward D. Sultan Company and sharing in its profits and losses. (R. 171.)

On the basis of these findings, the Tax Court, five judges dissenting, held that the Commissioner erred in including the Edward D. Sultan Trust's distributive share of partnership income in the income of the taxpayer and his wife. (R. 177-178.)

STATEMENT OF POINTS TO BE URGED

The points upon which the Commissioner relies as the basis for this proceeding are set forth at pages 187-191 of the record. In substance, they are that the Tax Court clearly erred in holding that the taxpayer did not retain sufficient control over the property which he had purportedly given away to remain taxable on the income attributable to that property and in holding that the donee-trust was the true owner-contributor of the gift capital upon which its claim of partnership status was based.

SUMMARY OF ARGUMENT

It is well established that the mere assignment of the right to receive income does not insulate the assignor

from tax liability. Accordingly, where the assignor of income-producing property actually retains control over that property and merely parts with the right to receive income therefrom, he is properly treated for tax purposes as the recipient of such income. Applying this principle in *Toor* v. *Westover,* this Court has held that a combination of a trust and a limited partnership may serve as the means by which an assignor retains control over property which he has purportedly given away. There the taxpayer assigned in trust for the benefit of his minor children property which the donee-bank was required to use to become and remain a limited partner in a partnership in which the taxpayer was the controlling general partner. This Court held that the taxpayer in that case remained the substantial owner of the assigned property because of the following crucial facts: (1) the donee was not free to remain out of the partnership, (2) the donee was not free to terminate the partnership or transfer its interest therein, and (3) the donor, as controlling general partner, retained the powers of management and full discretion as to time and amounts of distributions of profits. In the case at bar we have an almost identical factual pattern—the trustees were not free to remain out of the partnership; they were not free to terminate the partnership or transfer their interest as special or limited partner; the donor, as controlling general partner, retained the powers of management and control over the time and amounts of distributions of profits. The Tax Court erred, therefore, in holding that in transferring property in trust for the benefit of his minor son the taxpayer did not retain sufficient control over that property to be treated for tax purposes as the recipient of income therefrom.

To have acquired partnership status for tax purposes an alleged partner must have contributed to the partnership one or both of the ingredients of income—capital or services. Where partnership status is based solely on the contribution of gift capital, the alleged partner must have been the true owner-contributor of that capital. As a special or limited partner the trust in the case at bar could not have contributed services to the conduct of the partnership business. Moreover, it was not the owner-contributor of the gift capital because it was not free to withhold such capital from the partnership, to transfer its interest in the partnership, or to withdraw either the gift capital or the income attributable to it. The Tax Court erred, therefore, in holding that the trust was entitled to recognition as a partner for tax purposes.

ARGUMENT

I

The Tax Court Erred in Holding that in Transferring Property in Trust for the Benefit of His Minor Son the Taxpayer Did Not Retain Sufficient Control Over that Property To Be Treated for Tax Purposes as the Recipient of Income Therefrom

It is well settled that, no matter how skillfully the assignment may be devised, a taxpayer cannot avoid income taxes by assigning income-producing property and the income therefrom [3] if he retains sufficient control over either the property producing the income or the receipt of the income so produced to make it reasonable to treat him as the recipient of the income

[3] Of course, an assignment of income which will be or has been earned by the assignor's services is also ineffective to relieve him of tax liability. *Lucas* v. *Earl*, 281 U. S. 111; *Helvering* v. *Eubank*, 311 U. S. 122, rehearing denied, 312 U. S. 713.

for tax purposes. Thus, as stated by the Supreme Court in *Commissioner* v. *Sunnen,* 333 U. S. 591, 604:

> Nor is the tax problem with which we are concerned necessarily answered by the fact that such property, if it can be properly identified, has been assigned. The crucial question remains whether the assignor retains sufficient power and control over the assigned property or over receipt of the income to make it reasonable to treat him as the recipient of the income for tax purposes.

An assignor may retain control over the property producing the income or over the receipt of income so produced by any of a number of means or combinations of means. In each case the test whether such control has been retained depends upon the end result and not upon any isolated step or steps in a series of related transactions. *Helvering* v. *Clifford,* 309 U. S. 331; *Helvering* v. *Stuart,* 317 U. S. 154, rehearing denied, 317 U. S. 602; *Commissioner* v. *Sunnen, supra; Toor* v. *Westover,* 200 F. 2d 713 (C. A. 9th), certiorari denied, 345 U. S. 975; *White* v. *Fitzpatrick,* 193 F. 2d 398 (C. A. 2d). To be taxable on the basis of his retention of control over the income-producing property or over receipt of the income therefrom it is necessary only that the assignor have retained the right to exercise such control and not that he have actually exercised that right. *Helvering* v. *Stuart, supra,* pp. 170-171; *Commissioner* v. *Sunnen, supra.*

On its facts the case at bar most closely resembles *Toor* v. *Westover, supra.* That case involved a combination of trust and limited partnership agreements, under either of which alone the assignor might not have retained sufficient control to be taxed as the owner

of the income-producing property. This Court in its opinion, however, pointed out the significance of the package arrangement, holding that the assignor's control, stemming in part from the trust provisions and in part from the limited partnership agreement, was sufficient to render him taxable as the owner of the property which he had purportedly given away. In the case at bar we also have a package arrangement of a trust and a special or limited partnership. The majority of the court below in their analysis of the case, however, apparently did not focus on the end result of the partnership-trust arrangement but, treating each separately and ignoring or viewing as immaterial critical facts found by it, held that the parties to the original partnership agreement really and truly intended to join together for the purpose of carrying on the business and that under the provisions of the trust the taxpayer-settlor did not retain sufficient control to be treated as the recipient of the income for tax purposes. In this manner, we submit, the Tax Court reached a clearly erroneous conclusion.

In the *Toor* case a bank was the sole trustee for the taxpayer-settlor's minor children. There, this Court, disagreeing with the rationale of the District Court, pointed out (p. 716) that the question in issue turned on "whether in reality the bank as trustee for the minor children became the substantial owner of an interest in the capital of the alleged partnership." This Court then enumerated as follows the factors determining that question (pp. 716-717):

> Finding of Fact 15 in part states: "The partnership was not to terminate until 1955 and the interest of the limited partner was also stated to

be not transferable. But the plaintiff had the right to terminate the arrangement upon giving a thirty day notice of intention to dissolve it and he had the absolute right to purchase the interest of the limited partner at 'book' value." It thus appears that upon organization of the partnership the bank surrendered dominion over the money invested until 1955. It has been held that a family partnership will not fail merely because the donee is not free to dispose of his partnership interest. As said in *Middlebrook, Jr.,* 13 T. C. 385, where such a situation existed: "Partnership is a relationship arising out of contract. The partners may enter into an agreement between themselves with respect to their rights and interests which they deem proper." 13 T. C. at 394. In the instant case, however, *the donee was neither free to remain out of the partnership nor free to terminate or transfer his interest once the partnership was created.* The District Court's Finding of Fact 12 states: "The trust and limited partnership agreements were presented to the Bank by plaintiff as one package." We understand this to mean that the creation of the trusts was conditional upon organization of the partnership. Although the bank may have carefully investigated appellant and his business prior to assenting to becoming trustee, at no time subsequent to the creation of the trusts could the bank as trustee exercise independent judgment to determine whether it would or would not join in organizing the partnership. Because the bank was required to enter the partnership as a condition to creation of the trusts, and because of the further limitation that once the partnership was organized the bank was neither free to transfer its interest nor terminate the partnership, it cannot be said that the bank,

> as trustee, ever acquired such control as that which constitutes the usual attribute of property ownership. Considering these circumstances in connection with the fact that the appellant, as general manager, retained the powers of management and full discretion as to time and amounts of distribution of profits, we conclude that the appellant remained the substantial owner of the interest he purported to have given away. Cf. *Helvering* v. *Clifford,* 1940, 309 U. S. 331, 60 S. Ct. 554, 84 L. Ed. 788.

In the case at bar we have an almost identical factual pattern.[4] The donee in this case also "was neither free to remain out of the partnership nor free to terminate or transfer his interest once the partnership was created." The donee-trust was not free to remain out of the partnership because of paragraphs lettered (a) and (o) of the trust indenture. Paragraph lettered (a) provided that the trustees should use the entire amount transferred to them by the settlor to purchase a 42 per cent interest in the partnership and that they should continue to be a special or limited partner. (R. 52.) Paragraph lettered (o) provided that if court approval of such purchase and of the trustees' continuing to be a special partner was not obtained within 60 days, the trust indenture would be null and void. (R. 60-61.) The donee-trust was not free to terminate the partnership because of paragraphs numbered 11 and 18 of the special partnership agreement. Paragraph numbered 11 provided that the partnership

[4] The similarity should also be noted between the instant case and the cases of *Commissioner* v. *Brodhead,* No. 13,805, and *Commissioner* v. *Eaton,* No. 13,806, now pending on appeal to this Court, in each of which cases the taxpayers were represented by the same counsel and the same type of trust indentures and special partnership agreements were employed.

could be determined or terminated by a "majority in interest of the General Partners," defined therein to mean the taxpayer only. (R. 80.) Paragraph numbered 18, in its original form and as amended January 12, 1942, and February 2, 1945 (Exs. 7 and 9), provided that the general partners (the taxpayer and his brothers and sister) could continue the partnership indefinitely. (R. 87, 107, 121.) The donee-trust was not free to transfer its interest in the partnership because of paragraph numbered 8 of the special partnership agreement. Paragraph numbered 8 provided that the special or limited partner (the donee-trust) could assign its share or interest in the partnership only with the consent of the general partners who had full power and discretion to give or withhold such consent. (R. 78.) Moreover, paragraph numbered 7 of the special partnership agreement provided that, except as otherwise stated in the agreement, the determination of the taxpayer, as the owner of the majority in interest of the capital contributed by the general partners, would be binding upon the partnership and would establish the policy of the partnership (R. 77); paragraph numbered 4 provided that only such portion of the profits attributable to a partner's interest could be withdrawn from the partnership as the general partners might deem advisable (R. 75).[5] Thus, as stated in the opinion of the five judges dissenting below (R. 178):[6]

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[5] Paragraph numbered 4 provided that the amount of distributive net profits would be arrived at after deducting the compensation of general partners actively engaged in the business in amounts from time to time agreed upon by the general partners, constituting the reasonable value of their services. (R. 75.)

[6] The split decision of the Tax Court in the case at bar was referred to by this Court in *Toor* v. *Westover, supra.* There, this Court, pointing out that the cases were similar, stated (p. 717) that it was not persuaded by the reasoning of the Tax Court in this case.

> Here the trust was compelled to use the alleged gift to acquire an "interest" in the business; had no control of the property; could not sell or dispose of it; could not freely withdraw profits; was confined to its investment in the partnership business; and compelled to retain that investment unless the will of the general partners, including petitioner, permitted otherwise.

Accordingly, for tax purposes the assignor in the case at bar, as in *Toor,*[7] remained the substantial owner of the partnership interest which he purportedly had given away.

In *Helvering* v. *Horst,* 311 U. S. 112, the Supreme Court stated (p. 119):

> We have held without deviation that where the donor retains control of the trust property the income is taxable to him although paid to the donee.

The trust property in the case at bar was the taxpayer-settlor's demand note in the amount of $42,000. The trustees, however, did not acquire the usual attributes of ownership with respect to this property. They were required to invest it in the partnership; as a limited partner, they had no voice in the use of their investment; and they were not free either to withdraw or transfer their interest. The taxpayer-settlor, on the other hand, retained complete control over the trust property which he had purportedly given away. He was assured that it would immediately be returned for use in the business which he controlled. The partner-

[7] In the *Toor* case the trustee-bank apparently acted completely in a fiduciary capacity. In the instant case, however, paragraph lettered (l) of the trust indenture provided that the trustees would not be answerable or accountable for any loss or damage resulting from any act consented to by the taxpayer-settlor. (R. 59.)

ship which he dominated could also use it in any other business. Its use was to be without restriction by the donee-trust—because the donee-trust was only a special or limited partner. Its continued availability was assured because the donee-trust was not free to withdraw or transfer its interest. The other general partners were the taxpayer's own brothers and sister who also owed their interest to gifts from the taxpayer. He could at any time buy out any of the others at book value plus their share of undistributed profits. He could continue the partnership indefinitely and it could likewise be continued by his personal representative upon his death. Determinations of the taxpayer, as owner of the majority in interest of the capital contributed by the general partners, were binding upon the partnership and he established the policy of the partnership. By his purported transfer of property in trust for the benefit of his minor son, therefore, the taxpayer in reality [8] merely parted with the right to

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[8] Paul, Partnership in Tax Avoidance, 13 George Washington L. Rev. 121, 142-143 (1945):

> If we would truly orient the subject under discussion, we should recognize that the family partnership problem cannot be successfully treated as a local disease. Family trusts, family partnerships, family corporations, are in one sense all the same thing. They all may seek to reduce taxes by splitting, postponing, or otherwise controlling the receipt of taxable income without a substantial surrender of dominion by the person who would otherwise have to pay the tax. They may not change economic status, but merely present different facades. Substantial ownership, business, the operations of daily life, may go on as before. Lawyers who put aside their special interest as advocates, and their inherent fondness for legal subtleties, know that this is so. Taxation will not be the practical matter it is so often said to be until it develops a ruthless capacity to disregard the empty legalisms and the economic pretenses of the family partnership, the family trust, and even the family corporation, in favor of the facts of family life.

receive income from that property.[9] Of course, as stated by the Supreme Court in *Commissioner* v. *Sunnen, supra* (p. 604):

> It has long been established that the mere assignment of the right to receive income is not enough to insulate the assignor from income tax liability.

II

The Tax Court Erred in Holding that the Trust Was Actually the Owner-contributor of the Capital Necessary To Give It Recognition as a Special or Limited Partner for Tax Purposes

In *Commissioner* v. *Culbertson,* 337 U. S. 733, the Supreme Court held that in order to acquire partnership status for tax purposes, it is necessary not only that the alleged partner have contributed either services or capital to the partnership[10] but also that, where such

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[9] The taxpayer also even retained the right indefinitely to use that income since by virtue of paragraph numbered 4 of the special partnership agreement the maximum to which the trust was actually entitled was an account receivable which by virtue of paragraph lettered (d) of the trust indenture the trustees could ultimately turn over to the beneficiary. (R. 53, 75-76.) Use of trust property income already paid to the trustees was also made possible by the provision of paragraph lettered (g) of the trust indenture that the trustees could made loans to the partnership without liability for any resulting losses. (R. 56.) See Section 29.22(a)-21(e)(2) of Treasury Regulations 111, Appendix, *infra.* Further control by the taxpayer-settlor of the trust property income was contained in the provision of paragraph lettered (g) of the trust indenture that approval of the taxpayer-settlor was required for all investments of such income by the trustees. (R. 55-56.) This provision alone would be sufficient to render the trust property income for 1946 taxable to the taxpayer-settlor under Section 29.22(a)-21(e)(4) of Treasury Regulations 111, Appendix, *infra.*

[10] The opinion of the court below seems to emphasize the matter of intent almost to the extent of excluding any other requirement. While the intent of the parties is frequently the ultimate question in determining whether a family partnership arrangement is genuine, of course, parties do not become partners merely by intending to be such. Thus, in the language of the Supreme Court (pp. 739, 740):

> If it is conceded that some of the partners contributed neither capital nor services to the partnership during the tax years in

status is claimed on the basis of a contribution of gift capital, the alleged partner have been the true owner of that capital. Accordingly, the Supreme Court stated (p. 748):

> The cause must therefore be remanded to the Tax Court for a decision as to which, if any, of respondent's sons were partners with him in the operation of the ranch during 1940 and 1941. As to which of them, in other words, was there a bona fide intent that they be partners in the conduct of the cattle business, either because of services to be performed during those years, or because of contributions of capital *of which they were true owners, as we have defined that term in the Clifford, Horst, and Tower cases?* (Emphasis added.)

See also this Court's discussion of the legislative history of Section 340(b) of the Revenue Act of 1951, c. 521, 65 Stat. 452, in *Toor* v. *Westover, supra.*

In the case at bar the taxpayers have not contended that the trust, as a special or limited partner, did, or could under the laws of Hawaii, contribute services to the conduct of the partnership business. The partnership status of the trust, therefore, must rest upon the claim that it was the true owner, and therefore the contributor, of the gift capital. Of course, an alleged partner may be the true owner-contributor of gift capital if he voluntarily puts such capital in or voluntarily leaves it in the partnership. Here, however, as pre-

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question, as the Court of Appeals was apparently willing to do in the present case, it can hardly be contended that they are in any way responsible for the production of income during those years. * * * A partnership is, in other words, an organization for the production of income to which each partner contributes one or both of the ingredients of income—capital or services.

viously mentioned, the donee-trust had no option. It was not free to remain out of the partnership nor free to terminate or transfer its interest once the partnership was created. The gift of capital to the trust was conditioned upon the investment of that capital in the partnership. At the will of the general partners, among whom the taxpayer had the controlling interest, such capital, and also the income attributable to it, was to remain available for partnership use, a use with respect to which the trust, as a special or limited partner, had no voice. Under the circumstances, the trust was not the true owner of the gift capital. Accordingly, the trust was not entitled to recognition as a partner for tax purposes.

CONCLUSION

The decisions of the Tax Court are erroneous and should be reversed.

Respectfully submitted,

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AUGUST, 1953.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U.S.C. 1946 ed., Sec. 22.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b).

(26 U.S.C. 1946 ed., Sec. 182.)

Revised Laws of Hawaii (1935):

CHAPTER 225. PARTNERSHIPS, REGISTRATION OF.

SEC. 6870. *Between individuals.*—A partnership may be formed between two or more individuals for the transaction of any lawful business. A special

partnership may be formed between one or more persons, called general partners, and one or more persons called special partners, for the transaction of any business.

* * * * *

SEC. 6880. *Only general partners act.*—The general partners only shall have authority to transact the business of a special partnership.

SEC. 6881. *Special partners may advise*—A special partner may at all times investigate the partnership affairs and advise his partners or their agents as to their management.

SEC. 6882. *May loan money. Insolvency.*—A special partner may lend money to the partnership or advance money for it, or to it, and take from it security therefor, and as to such secured loans or advances has the same rights as any other creditor, but in case of the insolvency of the partnership all other claim which he may have against it must be postponed until all other creditors are satisfied.

SEC. 6883. *Receive interest and profits.*—A special partner may receive such lawful interest and such proportion of profits as may be agreed upon, if not paid out of the capital invested in the partnership by him or some other special partner, and is not bound to refund the same to meet subsequent losses.

SEC. 6884. *May not withdraw capital.* No special partner, under any pretense, may withdraw any part of the capital invested by him in the partnership during its continuance.

SEC. 6885. *Result of withdrawing capital.*—If a special partner withdraws capital from the firm, contrary to the provisions of sections 6883 or 6884, he thereby becomes a general partner.

Treasury Regulations 111, promulgated under the Internal Revenue Code:

> SEC. 29.22(a)-21 [as added by T. D. 5488, 1946-1 Cum. Bull. 19, and as amended by T. D. 5567, 1947-2 Cum. Bull. 9]. *Trust income taxable to the grantor as substantial owner thereof.*—
>
> * * * * *
>
> (e) *Administrative control.*—Income of a trust, whatever its duration, is taxable to the grantor, where, under the terms of the trust or the circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust. Administrative control is exercisable primarily for the benefit of the grantor where—
>
> * * * * *
>
> (2) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor to borrow the corpus or income, directly or indirectly, without adequate interest in any case, or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions; or
>
> * * * * *
>
> (4) any one of the following powers of administration over the trust corpus or income is exercisable in a nonfiduciary capacity by the grantor,

or any person not having a substantial adverse interest in its exercise, or both: a power to vote or direct the voting of stock or other securities, a power to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments, and a power to reacquire the trust corpus by substituting other property of an equivalent value.

* * * * *

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No. 13,804

IN THE

United States Court of Appeals

For the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

EDWARD D. SULTAN,
Respondent.

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

OLGA L. SULTAN,
Respondent.

On Petitions for Review of the Decisions of the Tax Court of the United States.

BRIEF FOR RESPONDENTS.

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On Petitions for Review of the Decisions of the Tax Court of the United States.

BRIEF FOR RESPONDENTS.

OPINION BELOW.

The opinion of the Tax Court (R. 159-178) is reported at 18 TC 715.

JURISDICTION.

The petitions for review in these cases involve deficiencies aggregating $406,452.34 in the federal

income taxes of the taxpayer Edward D. Sultan (herein called the "Taxpayer") and his wife[1] for the years 1944 through 1946 (R. 5, 26, 179-91). On April 26, 1949,[2] the Commissioner of Internal Revenue (herein called the "Commissioner") mailed to the Taxpayer and his wife notices of deficiencies in their income taxes for the years in question (R. 14, 34). Within 150 days thereafter, on August 12, 1949, the Taxpayer and his wife, pursuant to Section 272 of the Internal Revenue Code, filed petitions with the Tax Court for redetermination of such deficiencies (R. 4-24, 26-37). The proceedings were consolidated for hearing in the court below (R. 2, 4). On October 31, 1952, decisions of the Tax Court were entered redetermining the deficiencies (R. 179, 180). On January 10 and 19, 1953, the Commissioner filed his petitions for review invoking the jurisdiction of this court under Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948 (R. 181-87).

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[1]The Taxpayer's wife is involved only because of the community property law of Hawaii which became effective on June 1, 1945 (R. 160).

[2]There were added to the gross income of the Taxpayer and his wife for each of the years in question amounts in excess of 25 per cent of the gross income stated in their returns (R. 16, 19, 22, 35). Accordingly, under Section 275(c), Internal Revenue Code, assessment and collection of the deficiencies were not barred by the statute of limitations.

QUESTIONS PRESENTED.

1. Whether on all of the evidence in the record the Tax Court's finding of fact, that Edward D. Sultan, Ernest W. Sultan, Marie Hilda Cohen, Gabriel L. Sultan and Edward D. Sultan Trust really and truly intended to join together for the purpose of carrying on the business of Edward D. Sultan Co. and sharing in its profits and losses, is so unreasonable as to require a reversal of the decision below.

2. Whether the Tax Court erred in holding that in creating the Edward D. Sultan Trust, the Taxpayer did not retain sufficient interest in or control over the corpus or income thereof to render himself liable for income taxes or the income thereof.

STATUTES AND REGULATIONS INVOLVED.

The pertinent statutes and regulations are set forth in the Appendix, *infra.*

STATEMENT.

The Taxpayer does not controvert the Commissioner's statement of the case in the Brief for the Petitioner (herein cited "Brief") (pp. 3-13).

SUMMARY OF ARGUMENT.

The Commissioner does not here challenge the validity of the Edward D. Sultan Trust or of the special partnership agreement, under the law of the Territory of Hawaii, nor does he question the binding obligation thereof. Thus, the question is whether the special partnership should be recognized and given effect under the revenue laws of the United States. The test for determining that question has been formulated by the Supreme Court in *Commissioner v. Culbertson,* 337 U.S. 733, 93 L.ed 1659 (1949), and whether any given partnership measures up to that test is a question of fact. *Commissioner v. Culbertson,* 337 U.S. 733, 741-42, 93 L.ed 1659, 1664-65. A finding of fact by the Tax Court will not be disturbed on appeal unless it is clearly unreasonable. *Boehm v. Commissioner of Int. Rev.,* 326 U.S. 287, 293-94, 90 L.ed 78, 84-85 (1945); *Commissioner of Int. Rev. v. Scottish Am. Inv. Co.,* 323 U.S. 119, 123-24, 89 L.ed 113, 116-17 (1944); *Helvering v. Kehoe,* 309 U.S. 277, 279, 84 L.ed 751, 753 (1940). An examination of the record in the case at bar reveals not merely substantial basis for the Tax Court's finding on this question, but clear and persuasive evidence virtually compelling the conclusion at which the Tax Court arrived.

The income of a private express inter-vivos trust, although not payable to the settlor thereof, may be taxed to settlor under the revenue laws of the United States if the settlor retains a sufficient "bundle of rights" in the trust (*Helvering v. Clifford,* 309 U.S.

331, 84 L.ed 788 (1940)), as where a settlor creates a short term trust naming himself as trustee, grants himself broad discretion as to the income to be distributed, and retains a reversionary interest in the corpus of the trust. In the case at bar, however, the Taxpayer made an absolute irrevocable transfer in trust to independent trustees, had no control over the income of the trust, and possessed no reversion in the corpus thereof. Even under the special partnership agreement the Taxpayer had no control over the corpus or income of the trust which he could lawfully exercise for his own benefit. The doctrine of *Helvering v. Clifford, supra,* is clearly inapplicable to the instant case.

The Commissioner in his argument (Brief 13-15) reads into the opinion of this court in *Toor v. Westover,* 200 F.2d 713 (9th Cir. 1952), a departure from the test laid down by the Supreme Court in *Commissioner v. Culbertson, supra,* and seeks to establish a rule of law making the issue in family partnership cases one to be determined by the very kind of "objective tests" so clearly repudiated by the Supreme Court in *Commissioner v. Culbertson.*

ARGUMENT.

I.

THE EVIDENCE APPEARING IN THE RECORD CLEARLY SUPPORTS THE TAX COURT'S FINDING OF FACT THAT THE TAXPAYER, ERNEST W. SULTAN, MARIE HILDA COHEN, GABRIEL L. SULTAN AND THE EDWARD D. SULTAN TRUST REALLY AND TRULY INTENDED TO JOIN TOGETHER FOR THE PURPOSE OF CARRYING ON THE BUSINESS OF EDWARD D. SULTAN CO. AND SHARING IN ITS PROFITS AND LOSSES.

The Commissioner does not here challenge the validity of the Edward D. Sultan Trust or of the special partnership agreement under the law of the Territory of Hawaii, nor does he question the binding obligation thereof. Thus, the question is whether the special partnership should be recognized and given effect under the revenue laws of the United States. The test for determining that question has been formulated by the Supreme Court in *Commissioner v. Culbertson, supra,* in the following language:

> ". . . whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise. . . ." (337 U.S. 733, 742-43)

> ". . . If the donee of property who then invests it in the family partnership exercises dominion and control over that property—and through that control influences the conduct of the partnership and the disposition of its income —he may well be a true partner. Whether he is free to, and does, enjoy the fruits of the partnership is strongly indicative of the reality of his participation in the enterprise. . . ." (id. at 747)

A review of the record reveals ample support in the evidence for the Tax Court's finding on the question as posed in the *Culbertson* case.

A. *The Agreement.* The terms of the special partnership agreement (R. 71-90) clearly reflect the intent of the parties to join as partners in the enterprise. The first (unnumbered) paragraph of the agreement (R. 71-73) recites that the parties "do hereby form with each other a special partnership for the purpose of acquiring and thereafter conducting the business heretofore carried on by Edward D. Sultan . . . and for other purposes . . . ." which purposes are spelled out in detail in paragraph 1 (R. 71-73).

Paragraph 3 of the agreement (R. 73-75) sets forth the respective capital contributions of the partners and secures to the special partner all of the powers, rights and duties of special partners as prescribed by Chapter 225 of the Revised Laws of Hawaii 1935 (see Appendix, *infra*) as the same might from time

to time be amended. The same paragraph provides that the special partner shall not be liable for the debts of the partnership beyond the limits set by Section 6887 of the Revised Laws of Hawaii 1935 (see Appendix, *infra*) as the same might from time to time be amended.

Paragraph 4 of the agreement, both as originally adopted and as amended, provides for compensation for services rendered to the partnership by the general partners actively engaged in the business of the partnership, and provides that such compensation shall be chargeable as an expense of the business for the purposes of computing the net profits of the partnership (R. 75, 111). The same paragraph provides for annual division of the net profits of the partnership in direct proportion to the stated capital interest of each of the partners and permits any partner to withdraw such portion of his profits as the general partners may from time to time deem advisable (R. 75, 111). It also provides that any profits not so withdrawn shall be credited to advance accounts in the names of the respective partners for whom such profits are being held, which accounts shall bear interest at the rate of five percent per annum computed on quarterly balances (R. 75, 76, 111, 112).

Paragraph 7 of the agreement expressly recognizes the right of the special partner to investigate the partnership affairs and advise the general partners as to its management at all times (R. 77).

Paragraph 9 of the agreement requires that proper partnership books of account be kept, and expressly confers upon each partner the right at all times to have full and free access to and to make copies of the partnership books (R. 78-79).

Paragraph 10 of the agreement requires annual general accounts to be taken of all of the assets and liabilities and dealings and transactions of the partnership and expressly requires that copies of such accounts be sent to each partner (R. 79-80).

Paragraph 8 of the agreement provides that if any partner were to make any additional capital contribution to the partnership, every other partner would have the right to make like contributions in order to keep the interest of each partner in the partnership in proportions equal to those in existence at the date of its inception (R. 78).

Although pursuant to paragraph 8 no general partner could assign or mortgage his or her share of or interest in the partnership or its assets or profits (except to another partner), the special partner was free to assign its interest in the partnership with the consent of the general partners (ibid.).

Paragraph 11 of the agreement (R. 80-81) provides that upon the determination of the partnership from whatever cause, the assets of the partnership remaining after payment of its debts and expenses shall be applied first to the payment of the balance due to the special partner as shown on its advance account

(before being applied to the payment of the balance due any general partner as shown in his or her advance account), and then in payment of the special partner's share of the capital (before being applied in payment of the share of capital of any general partner).

B. *The Conduct of the Parties.* The evidence in the record concerning the conduct of the parties in pursuance of the partnership agreement clearly reflects the intent of those parties to join together for the purpose of carrying on the enterprise and sharing in its profits and losses.

Taxpayer and his brother, Ernest W. Sultan, both general partners, rendered services to the partnership in accordance with paragraph 5 of the partnership agreement (R. 203-04, 225-26). For these services Taxpayer and Ernest W. Sultan were paid reasonable compensation, to which all of the partners appear to have consented, and such compensation was deducted as an expense of the partnership business in computing the profits thereof (R. 204-06, 209, 233, 238-39).

The general partners consulted together and discussed the business policies among themselves very extensively (R. 232). The special partner investigated the partnership affairs and advised the general partners as to its management in accordance with the partnership agreement and with the applicable law. In this connection the Taxpayer's uncontra-

dicted testimony, fully corroborated by that of the trust officer in charge of the Edward D. Sultan Trust (*infra,* pp. 11-12) shows that the Taxpayer consulted regularly with the special partner, furnished it regular accounts of the conduct of the business, and gave interim accounts of the status of the business (R. 214-15). The special partner was advised with respect to changes in salary for the Taxpayer and for Ernest W. Sultan, and expressed its agreement thereto (R. 233).

The testimony of the trust officer who succeeded to the responsibility for the Edward D. Sultan Trust account shows that the special partner consulted with the Taxpayer as to how the business was going, as to the difficulty of obtaining shipments due to the war, and as to the growth of the business (R. 252-53). That testimony further shows active consultation and advice by the special partner with respect to the sale of its partnership interest by the special partner (R. 254-55); discussions of the business between the special partner and the Taxpayer periodically three or four or five times a year; and participation in discussions concerning the adoption of various and sundry policies by the partnership (R. 257-58). Audit reports and oral reports were furnished to the special partner regularly and promptly (R. 215).

With the exception of certain periods when with the consent and agreement of the special partner certain partnership profits were retained in the business to permit the accumulation of additional capital,

the special partner was adamant in its insistence upon full and prompt distribution of its distributive share of the partnership profit (R. 49, 156, 211, 228, 254-55, 259-61).

When the special partnership was dissolved through the purchase by the Taxpayer of the interests of the other partners, the purchase price of those respective interests followed exactly the percentage allocation of capital as determined by the partnership agreement (R. 47, 48, 137-54, 210-12, 239-40).

The parties to the special partnership agreement, including the Edward D. Sultan Trust, held themselves out to the public as general and special partners respectively by filing in the Office of the Treasurer of the Territory of Hawaii a duly executed certificate of special partnership and affidavits of each of the partners, and by publishing a statement of substance of certificate of special partnership in the Honolulu Advertiser on four different days (R. 45, 94-105). In addition, upon its termination the respective members of the special partnership gave public notice of the dissolution of the special partnership and the termination of their partnership relationship by filing a statement thereof in the Office of the Treasurer of the Territory and by publishing notice of dissolution in the Honolulu Advertiser on four different days (R. 48, 49, 149-54).

Each of the general partners other than the Taxpayer became a member of the special partnership by reason of his or her particular qualifications and

contribution to the business (R. 44, 71-90, 199-201), and it is significant that the Commissioner does not assert that they were not bona fide members of the special partnership.

C. *The Relationship of the Parties.* The evidence in the record with respect to the relationship of the parties lends ample support to the Tax Court's finding. Each of the Taxpayer's brothers and sister who joined as a general partner in the conduct of the partnership business had been associated in the wholesale jewelry business in one aspect thereof or another. Ernest W. Sultan had been manager of the Taxpayer's sole proprietorship in the past (R. 194-95), Marie Hilda Cohen had aided by furnishing warehousing space on the west coast (R. 200), and Gabriel L. Sultan had acted as a sales representative on the mainland (R. 200-01). The trustees of the Edward D. Sultan Trust (of which the Taxpayer's son was the beneficiary) maintained at all times a relationship of independent arm's length dealing with the general partners. The corporate trustee exercised its independent judgment in deciding whether to become a special partner, even insisting upon approval by court of competent jurisdiction before it would accept the trusteeship (R. 252). It insisted upon prompt and full withdrawals of its partnership earnings (R. 211, 228, 254-55, 259-61) and exercised its independent judgment on partnership affairs (R. 254-55, 264) including the sale of its partnership interest (R. 264).

D. *Abilities and Contributions of the Parties.* An examination of the evidence in the record relating

to the respective abilities and contributions of the parties indicates ample support for the Tax Court's finding. The Taxpayer had been in the jewelry business or in the manufacturing jewelry business practically all of his life since he was ten years old (R. 194), and he contributed both capital (R. 74, 91-94) and services (R. 203-04, 225-26) to the partnership enterprise.

General partner Ernest W. Sultan had had considerable experience as office manager of the sole proprietorship and had knowledge of the jewelry business far above that of the Taxpayer (R. 221-22). He contributed both capital (R. 74, 91-94) and services (R. 225-26) to the partnership enterprise.

General partner Marie Hilda Cohen was a capable business woman and ran a business in San Francisco with her husband (R. 199-200, 218). She contributed both capital (R. 74, 91-94) and warehousing services to the partnership enterprise.

General partner Gabriel L. Sultan was an experienced jewelry salesman, having previously acted as mainland salesman for the sole proprietorship (R. 200-01, 218-20). He contributed capital to the partnership enterprises (R. 74, 91-94) and was only prevented from furnishing services by circumstances arising out of World War II and beyond the control of any of the partners (R. 218-20).

Bishop Trust Company, Limited, conducted a trust company business in the Territory of Hawaii and had enjoyed wide experience in operating business

enterprises in a fiduciary capacity. Among the varieties of businesses operated by Bishop Trust Company, Limited, were included a structural steel business, a department store, a tile business, dairies, ranches, an ice cream business, a soda and ice works which held the Coca-Cola franchise for one of the Hawaiian Islands, and an auto sales agency (R. 248-51). As co-trustee with Ernest W. Sultan, it contributed capital to the partnership enterprise (R. 74, 91-94) and contributed advice and consultation to the full extent permitted by law on the part of a special partner (R. 214, 233, 252-53, 254-55, 257).

Capital was a significant income producing requirement of the partnership business. The partnership paid all invoices immediately upon shipment of the goods covered even though the goods were not received until much later (R. 207-09), and indeed the general partners left their earnings in the special partnership in order to assure that sufficient capital would be available to make such payments (R. 209). The Taxpayer made continual loans of large sums to the partnership business without interest in order to build up the capital funds (R. 211). As the testimony of one of the trust officers in charge of the Edward D. Sultan Trust indicates, the special partner was aware of the need for substantial capital in the business and gave its careful attention to the problem (R. 252-53, 254-55, 263-64), temporarily permitting its partnership profits to be retained in order to improve the credit rating of the special partnership (ibid.).

E. *Actual Control of Income.* The evidence in the record with respect to the exercise of actual control over the special partnership income fully supports the Tax Court's finding that the parties thereto really and truly intended to join as partners in the conduct of the special partnership business. As shown above (p. 12), the special partner firmly insisted upon withdrawing, and promptly withdrew, the entire amount of its distributive share of the special partnership net profits. When it was desired to retain some of the partnership profits, the consent of the special partner was first obtained (R. 263-64). During the entire period of the existence of the special partnership, the special partner received and held under its sole and exclusive dominion and control its entire distributive share of the special partnership income and none thereof was ever paid to the Taxpayer or used in discharge of his obligations to support his wife or his child (R. 155, 263-64, 215).

F. *Business Purpose.* The purpose of preserving and continuing a going business as a family enterprise for the members of a family is a proper, legitimate and indeed a commendable business purpose. *Ardolina v. Commissioner of Internal Revenue,* 186 F.2d 176 (3d Cir. 1951); *Nicholas v. Davis,* 204 F. 2d 200 (10th Cir. 1953). The uncontradicted testimony of the Taxpayer clearly indicates that the special partnership was entered into for the purpose of assuring the continuity of the business and of interesting the Taxpayer's son in the business in order that it might

have the benefit of his subsequent participation, as well as to assure the availability of necessary warehousing space and sales representation on the mainland of the United States (R. 195-201, 217-20). That testimony further clearly indicates the absence of any motive of tax avoidance or desire to reallocate income within the family group (R. 198, 230-32).

G. *Dominion and Control of Special Partner's Interest.* The Edward D. Sultan Trust was the donee of property in the amount of $42,000.00, as is shown by the Commissioner's determination that the Taxpayer made a completed absolute gift to the trust upon its creation in 1941, the Commissioner's determination that the value of the gift was greater than $42,000.00, and his assessment of a deficiency in gift tax on that account (R. 45-46), and as is more fully demonstrated under Point II, *infra*, which discussion is herein incorporated. And the Edward D. Sultan Trust invested the property given to it in the special partnership (R. 51-62, 63-70, 71-90, 91-94).

The trust, as donee of the property which it had invested in the special partnership as a special partner, was clothed with all of the dominion and control permissible in a special partner under the law of the Territory of Hawaii (R. 73-75) and by its exercise of such dominion and control, it influenced the conduct of the partnership to the full extent that a special partner lawfully could do so (R. 214, 233, 252-53, 254-55, 257). It did not merely influence the disposition or special partnership income, but insisted upon full

and prompt payment of all of the distributive share of special partnership income allocable to it under the terms of the special partnership agreement (R. 49, 156, 211, 228, 254-55, 259-61). The record clearly indicates that the special partner enjoyed the "fruits of the partnership" to the very fullest.

From the foregoing review of the evidence appearing of record in the case at bar, it is obvious that there is more than sufficient support for the Tax Court's finding of fact that the Taxpayer, Ernest W. Sultan, Marie Hilda Cohen, Gabriel L. Sultan and the Edward D. Sultan Trust really and truly intended to join together for the purpose of carrying on the business of Edward D. Sultan Co. and sharing in its profits and losses.

II.

THE INCOME OF THE TRUST IS NOT TAXABLE TO THE TAXPAYER UNDER THE DOCTRINE OF HELVERING v. CLIFFORD OR THE COMMISSIONER'S REGULATIONS RELATING THERETO.

In *Helvering v. Clifford,* 309 U.S. 331, 84 L.ed 788 (1940), settlor created a trust for a term of five years with the proviso that it would terminate earlier on the death of either settlor or his wife with himself as trustee and his wife as income beneficiary. On the termination of the trust the entire corpus was to revert to the settlor while accrued or undistributed net income and net proceeds from the investment of

any such net income was to be treated as his wife's absolute property. During the continuance of the trust settlor was to pay over such part of the income therefrom as he in his absolute discretion might determine, and during that period he had full power to exercise all voting rights incident to the trusteed shares of stock, to sell, encumber or otherwise dispose of any part of the corpus or income on such terms as he in his absolute discretion deemed fitting, and to invest any of the property of the trust by loans, secured or unsecured, by deposits in banks, or otherwise, without restriction as to the speculative character or rate of return of any such investment, or of any laws pertaining to the investment of trust funds. The Supreme Court, holding the settlor taxable on the income of the trust, in addition to the family relationship of the settlor and the beneficiary, emphasized the following factors: The short term of the trust, the fact that settlor was also the trustee, the absolute discretion in the settlor-trustee as to income to be distributed, and the reversion to the settlor upon the termination of the trust.

Underlying the decision of the Supreme Court in the *Clifford* case is the principle that where a purported donor retains controls over the subject matter of his gift, exercisable for his own personal benefit, sufficient to afford him the economic use and benefit of the property to substantially the same extent as if he were the absolute owner thereof, then the donor should remain taxable upon the income of that property.

An examination of the trust deed in the case at bar shows that with the exception of the close family relationship between settlor and beneficiary, none of the factors considered in the *Clifford* case is present here.

The term of the trust is to continue until the Taxpayer's son, who was between thirteen and fourteen years of age at the inception of the trust (R. 43, 51, 52), reaches the age of thirty years or sooner dies (R. 53-54). Thus, the maximum term of the trust was just over sixteen years.

The Taxpayer in the case at bar did not name himself a trustee of the Edward D. Sultan Trust. Instead, he carefully selected his brother, Ernest W. Sultan, and Bishop Trust Company, Limited, as trustees in order to take advantage of their experience and knowledge (R. 51, 196-99). Moreover, he named his sister, Marie Hilda Cohen, successor trustee to Ernest W. Sultan, and provided that in the event both Ernest W. Sultan and Marie Hilda Cohen should be or become unable to act or decline to act or resign as trustee, then Bishop Trust Company, Limited, should act as sole trustee (R. 59).

Any suggestion that Taxpayer's brother in his capacity as co-trustee would be or was under the domination of the Taxpayer loses its force by reason of the fact that under the trust deed and the applicable law, the concurrence of both trustees would be required on all decisions. 2 *Scott, Trusts,* Sec. 194 (1939).

Since the Taxpayer was not a trustee of the Edward D. Sultan Trust, it is self-evident that he could not under the trust deed control the distribution or other disposition of the income therefrom.

The Taxpayer held no reversionary interest whatever in the corpus or income of the Edward D. Sultan Trust. Upon the termination of the trust, the trust property was to be distributed in the manner set out in the trust deed (R. 53-54) to the Taxpayer's son or, if he were not then living, to the Taxpayer's wife or, if she were not then living or in certain other circumstances, to the named brothers and sister of the settlor, or, if any of them were not living, to his or her issue.

Thus, it is evident that none of the factors emphasized by the Supreme Court in the *Clifford* case and repeatedly re-emphasized by the lower courts is present in this case.

Treasury Regulations 111, Section 29.22(a)-21[3] (herein called the "Clifford Regulations"), embody the Commissioner's exegesis upon the doctrine of *Helvering v. Clifford, supra,* and is applicable only to taxable years beginning on and after January 1, 1946. The Commissioner in his argument (Brief 23, n. 9) suggests in passing that the 1946 income of the trust might be taxable to the Taxpayer under either or both of Sections 29.22(a)-21(e)(2) and 29.22(a)-21(e)(4). Section 29.22(a)-21(e)(2) asserts the Commissioner's

[3]TD 5488, 1946-1, Cum. Bull. 19;
TD 5567, 1947-2, Cum. Bull. 9.

opinion that income of a trust, whatever its duration, is taxable to the grantor where, under the terms of the trust or the circumstances attendant upon its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust through a power exercisable by the grantor or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor to borrow the corpus or income directly or indirectly without adequate interest in any case or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions. Section 29.22(a)-21(e)(4) states the Commissioner's similar opinion with respect to a power exercisable by the grantor in a non-fiduciary capacity to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments.

The Commissioner suggests here that the terms of the trust permitting the trustees to make loans to the partnership without liability for any resulting losses (R. 56) and providing that during the lifetime of the Taxpayer the trustees shall obtain the consent of the Taxpayer to the making of investments other than investments which trustees are permitted by law to make, render the 1946 income of the trust taxable

to the Taxpayer by the force of the Clifford Regulations. The Commissioner's error in this respect arises largely from the fact that, assuming as his major premise the result for which he contends, namely, that the special partnership, Edward D. Sultan Co., was a mere sham not entitled to recognition for income tax purposes, the Commissioner reasons that the Taxpayer and the partnership were one and the same entity for all purposes.

Without conceding the validity of the Clifford Regulations, the Taxpayer contends that those regulations are inapplicable in the case at bar. The trustees' power to make loans to the partnership of Edward D. Sultan Co. is a far different thing from a power to make loans to the Taxpayer. Any such loan would be to the partnership and for the partnership's account and not to the Taxpayer personally or for his personal benefit. As a partner in Edward D. Sultan Co., the Taxpayer stood in a fiduciary relation to each of the other partners, including the special partner. The Supreme Court of the Territory of Hawaii has recently reaffirmed in the strongest terms the proposition that there is scarcely any relation in life which calls for more absolute good faith than the relationship of partners, and that the obligation is even greater in the case of a managing partner. *Watumull v. Ettinger,* Sup. Ct., T. H., Jan. 3, 1952; see also *Toor v. Westover,* 200 F. 2d 713, 715 (9th Cir. 1952).

Assuming that a loan had been made from the trust to the partnership (and the record reveals no such

loan), the Taxpayer could only have diverted the proceeds of the loan to his personal use and benefit by a violation of his clear and unambiguous duty as a partner, which violation would give rise to a cause of action in favor of the trust and all other partners not participating therein against the Taxpayer. *Watumull v. Ettinger, supra.* The proposition that the naked power to seize property in violation of law renders the holder of that power taxable on the income of that property has never been seriously advanced.

In his argument from the requirement of consent to non-legal investments by the Taxpayer, the Commissioner overlooks the fact that the very terms of the Clifford Regulations restrict their applicability to a power exercisable *in a non-fiduciary capacity.* Under the doctrine of the *Clifford* case, a mere power to direct or veto proposed investments not exercisable for the benefit of the grantor does not render the holder of the power taxable on the income of the trust property.

In *Cushman v. Commissioner of Internal Revenue,* 153 F.2d 510 (2d Cir. 1946), petitioner created an irrevocable trust for the benefit of his children, naming himself and his wife as co-trustees with a corporate successor trustee. The petitioner reserved to himself, as grantor, the power to control retention or sale of trust property and to direct investment or reinvestment of trust funds. The Commissioner determined that the trust income was taxable to the

petitioner under the doctrine of the *Clifford* case, and the Tax Court agreed. On appeal to the Court of Appeals for the Second Circuit, the decision of the Tax Court was reversed. In answer to the Commissioner's contention, the court held that the petitioner's reserved power to control retention or sale of trust property and to direct investment and reinvestment of trust funds did not suffice to bring the case within the doctrine of *Helvering v. Clifford,* since the powers so retained could not be used contrary to the best interests of the beneficiary of the trust. Judge Chase, writing for the court, pointed out that ordinarily such powers are held in a fiduciary capacity and their exercise is subject to the scrutiny of the courts.

Again, in *Kohnstamm v. Pedrick,* 153 F.2d 506 (2d Cir. 1945), an appeal from a judgment dismissing the complaint entered after trial upon stipulated facts in the District Court for the Southern District of New York, plaintiff had created a trust for the benefit of his wife and children and had reserved to himelf, as grantor, the power, among others, to direct the sale of any part of the trust fund and substitute equivalent investment and to vote all shares of stock held by the trust. Judge Learned Hand, writing for the court, in reversing the decision below, held that the power to direct the sale of trust assets and substitute equivalent instruments, even when coupled with the other powers reserved, did not bring the plaintiff within *Helvering v. Clifford* and make him

the owner of the trust property for tax purposes. See also *William P. Anderson,* 8 TC 921 (1947), acq. 1947-2 Cum. Bull. 1; *Arthur L. Blakeslee,* 7 TC 1171 (1946), acq. 1947-1 Cum. Bull. 1; *David L. Loew,* 7 TC 363 (1946); *Ernst Huber,* 6 TC 219 (1946), acq. 1946-1 Cum. Bull. 3.

The very terms of the trust deed in the case at bar (R. 55-56) negative any inference that the power reserved by the Taxpayer to require his consent to the making of certain investments during his lifetime is reserved for the benefit of anyone other than the beneficiary of the trust. The trust deed confers upon the trustees power to invest in property, real or personal, insofar as in their judgment they shall deem such investments advisable, and recites that in making such investments, the trustees shall not be restricted to investments which are legal for trust funds. The proviso reserving the power to require the Taxpayer's consent follows immediately after this grant and clearly relates to the making of investments which are not legal for trust funds. In every instance during the life of the Taxpayer, proposed investments must be investments which, in the judgment of the trustees, are advisable for the trust—that is, investments which are in the best interests of the income beneficiary and remainderman under the trust.

Thus, even if the Clifford Regulations are valid and applicable, the Taxpayer is not taxable upon the trust income by the force of those regulations.

If the Clifford Regulations are applicable, a determination that the 1946 income of the trust is taxable

to the Taxpayer by the force of the regulations must result in the conclusion that the regulations as applied are invalid. As has been demonstrated above, the Taxpayer is not taxable upon the income of the trust under the doctrine of *Helvering v. Clifford* alone. If the Taxpayer is held taxable on the 1946 income of the trust without any change in the facts or in the applicable law, then the regulations are invalid for the reasons stated in *Commissioner of Internal Revenue v. Clark,* 202 F.2d 94 (7th Cir. 1953). In that case the taxpayers created irrevocable trusts for the term of five years, subject to extension by the grantors. Thereafter and for good cause, the grantors extended the irrevocable term of the trusts for at least five additional years, all other provisions remaining unchanged. The Commissioner assessed the 1946 income of the trusts to the grantors on the theory that the terms of the trusts were of less than ten years' duration and hence the income thereof was taxable to the grantors under the Clifford Regulations. The Tax Court held that the 1946 income of the trusts was not taxable to the grantors under Section 22(a) of the Internal Revenue Code or under *Helvering v. Clifford, supra,* or under the Clifford Regulations. On appeal by the Commissioner the Court of Appeals for the Seventh Circuit, affirming the decision of the Tax Court, held that the Clifford Regulations as applied in that case were unreasonable and arbitrary and therefore void. Chief Judge Major, for the court, pointed out that the regulation created a conclusive or irrebuttable pre-

sumption and thus stated a rule of substantive law. Hence, without any alteration in the trust indentures and without any change in the relation of any of the parties thereto, that which was not income taxable to the grantors in 1944 and 1945 became income taxable to the grantors in 1946 solely as a result of the promulgation of the Clifford Regulations. Referring to cases in which the Supreme Court struck down as violative of due process a state statute which provided, in effect, that gifts of a decedent's estate made within six years of his death were made in contemplation thereof[4] and a congressional enactment which created a conclusive presumption that gifts made within two years prior to the death of the donor were made in contemplation of death,[5] Chief Judge Major stated that it appears that even Congress would be without power to create the conclusive presumption which the Treasury had attempted to create in the Clifford Regulations, and that it was even more certain that an administrative agency is without authority to promulgate such a regulation.

Exactly the same situation would exist in the case at bar if the trust income were taxed to the Taxpayer by the force of the Clifford Regulations. There was no significant change in the provisions of the trust deed between the years preceding and the year 1946. The Clifford Regulations create a conclusive or irrebuttable presumption, a rule of substantive law, effec-

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[4]*Schlesinger v. Wisconsin*, 270 U.S. 230, 70 L.ed 557 (1926).
[5]*Heiner v. Donnan*, 285 U.S. 312, 76 L.ed 772 (1932).

tive on and after January 1, 1946, that the existence of a power in the grantor to borrow corpus or income or of a power in a non-fiduciary capacity to veto proposed investments makes the income of a trust the income of the grantor thereof. For the reasons set forth in *Commissioner of Internal Revenue v. Clark, supra,* any such application of the Clifford Regulations to the case at bar would be arbitrary, unreasonable and void.

Thus, the terms of the trust and the circumstances of its creation demonstrate that the income thereof is not taxable to the Taxpayer under the doctrine of *Helvering v. Clifford* or the extension of that doctrine embodied in the Clifford Regulations.

A consideration of the terms of the trust and the circumstances of its creation together with the terms of the special partnership agreement and the operations of the special partnership leads to a like conclusion. The term of the special partnership agreement was initially from August 30, 1941, to April 30, 1943, and thereafter from year to year unless terminated (R. 71, 87). As amended January 12, 1942, the special partnership agreement provided that after the death of the Taxpayer, the agreement should continue in full force and effect until the end of the fiscal year of the business of the partnership ending in 1953 (R. 107). As amended February 2, 1945, the agreement provided that the term of the partnership should be for a period commencing February 2, 1945, and ending January 31, 1946, and thereafter from

year to year until terminated (R. 121). The term of the special partnership agreement, however, had no effect upon the term of the trust, and on termination of the partnership agreement, the Taxpayer could not receive any part of the special partner's share of capital or of earnings. Indeed, the special partner was granted priority in distribution on termination (R. 80-81).

The Taxpayer was the general partner with the majority interest in the special partnership, but, as pointed out above (pp. 20-26), his powers as such were not and could not lawfully be exercised for his own personal benefit. Under the rule laid down by the Supreme Court of the Territory of Hawaii in *Watumull v. Ettinger, supra,* the Taxpayer owed a duty of absolute good faith to his partners, including the special partner. See also *Toor v. Westover, supra.* Nor could the Taxpayer, as general partner with the majority interest in the special partnership, cause the assets of the special partnership to be diverted to any personal business of the Taxpayer. True, the special partnership agreement permitted the partnership to enter into a broad field of activity, but any business carried on by the partnership would be for the benefit and account of the partnership and of each of the partners therein.

Under the special partnership agreement, the Taxpayer had no power over the income of the partnership exercisable for his own benefit. While he held the power to determine the compensation of the gen-

eral partners actively engaged in the business of the partnership, including himself (R. 75), by the very terms of the grant of that power, the compensation for services was restricted to "the reasonable value of the services rendered to the partnership" (ibid.). Had the Taxpayer attempted to cause himself to be paid an unreasonably large salary for his services to the partnership (and there is no evidence in the record of any such attempt), he would have violated his absolute duty of good faith to the partners including the special partner, and would have been held to account under the rule of *Watumull v. Ettinger, supra.*

Similarly, partners' withdrawals from the partnership of the profits attributable to their interests was subject to the control of the Taxpayer as general partner with the majority interest in the partnership. Here again, any retention of partnership earnings (and the record indicates that none of the special partner's earnings were retained without its consent) would inure to the benefit of the partnership and all of the partners therein, and any attempt on the part of the Taxpayer (and the record indicates no such attempt) to withhold the earnings of the special partner or of any other partner for his own personal use or benefit would constitute a violation of the rule laid down in *Watumull v. Ettinger, supra,* and render the Taxpayer accountable therefor. To contend that the existence of this power renders the Taxpayer taxable on the special partner's distributive share of the part-

nership income is once again to assert that the naked power to seize property in violation of law makes the holder of that power liable for taxes on the income of the property.

Nor could the Taxpayer obtain control of the corpus of the trust for his own use or benefit. The Commissioner in his argument states that the Taxpayer "could at any time buy out any of the others at book value plus their share of undistributed profits" (Brief 22). This statement is without foundation in the record and is contrary to the fact. The Taxpayer, as the general partner with the majority interest in the partnership, could terminate the special partnership at any time upon certain written notice (R. 80). In the event of such termination, however, the assets of the special partnership, after payment of its debts and expenses, were to be distributed to the partners in the proportion to their capital contributions, and the special partner was afforded priority in this distribution (R. 80-81). If any other general partner were to die or give notice of termination during the term of the special partnership agreement, then and only then the Taxpayer could purchase the interest of the deceased general partner at the fair value thereof (R. 83-84, 118-20). The Taxpayer, as general partner with the majority interest in the special partnership, could use the assets of the partnership in the partnership business and share in the profits and losses thereof, but he could not, without violating his duty of absolute good faith to his other partners divert those assets

to his own personal business or to any other business. *Watumull v. Ettinger, supra.* Similarly, the option granted to the Taxpayer's representative to succeed to or carry on the interest of the Taxpayer in the business in the event of the Taxpayer's death, either as a general partner or as a special partner, would afford to the Taxpayer's estate no power to divert the partnership assets to the benefit of the estate, and all of the acts of the Taxpayer's representative upon succession to the Taxpayer's interest in the partnership would be governed by the same duty of absolute good faith which governed the Taxpayer during his lifetime.

Thus it is clear that under the doctrine of the *Clifford* case, the trust deed and special partnership agreement taken together with the circumstances surrounding the same did not reserve to the Taxpayer any power sufficient to render him taxable upon the income of the trust or the special partner's distributive share of the partnership income.

It is clear from the Commissioner's argument (Brief 15-25) that he asserts the income in question to be taxable to the Taxpayer solely under the doctrine of *Helvering v. Clifford, supra,* and relies almost exclusively upon the language of the opinion of this court in *Toor v. Westover, supra.* The Commissioner's only challenge to the bona fides of the special partnership is based on his assertion that the trustees did not become the real owners of the trust property (Brief 23), and if this contention fails, his entire argument falls.

The Commissioner maintains that the trustees "did not acquire the usual attributes of ownership with respect to this property" (Brief 21), and lists twelve propositions in support of this contention. That these twelve propositions, to the limited extent that they have a basis in the law or the record, do not lead to the conclusion contended for, appears from the following seriatim examination thereof:

1. ". . . They were required to invest it in the partnership. . . ." (Brief 21) The Commissioner's position here appears to be that a transfer of property in trust wherein the trustee is not granted the power of sale, but is directed to retain the property so transferred, cannot so shift the ownership of the property as to render the trustee or the trust beneficiaries taxable upon the income thereof. On this theory a transfer or gift of a partnership interest would never be effective to shift the incidence of taxation, since the donee would have no choice but to become a partner or refuse the gift. Simply to assert these propositions is to accomplish their refutation.

2. ". . . as a limited partner, they had no voice in the use of their investment. . . ." (Brief 21) This statement simply is not borne out by the law, the special partnership agreement or the record. As pointed out above, the trustees were granted all of the voice in the use of their investment that it was possible to grant to a special partner under the law of the Territory of Hawaii, and they exercised their rights to the fullest. There is no doubt that a special

or limited partner may be recognized under the revenue laws of the United States as a bona fide partner in a special or limited partnership. *Nicholas v. Davis,* 204 F.2d 200 (10th Cir. 1953); *Toor v. Westover, supra; John A. Morris,* 13 TC 1020 (1949), acq. 1950-1 Cum. Bull. 3; *Walter R. Stutz,* 10 TCM 506 (1951); *William Collins, Sr.,* 7 TCM 803 (1948); *Jacques Spira,* 7 TCM 371 (1948).

3. ". . . they were not free either to withdraw or transfer their interest. . . ." (Brief 21) This statement is not altogether free from its misleading elements inasmuch as the special partner was not *absolutely* free to withdraw or transfer its interest, but was free to make such withdrawal or transfer with the consent of the general partners (R. 78). It may be noted that no general partner was free to assign his interest except to another partner under any circumstances (ibid.). The Commissioner apparently concedes that restriction on the transferability of a partner's interest is not fatal to the existence of a bona fide partnership, for he quotes with approval (Brief 18) the language of this court in *Toor v. Westover, supra,* to that effect. See also *Joseph Middlebrook, Jr.,* 13 TC 385 (1949), acq. 1950-1 Cum. Bull. 3; *William Collins, Sr., supra.* Nothing in the language of the Supreme Court in *Helvering v. Clifford* would indicate that the donor of all or a part of a special partner's interest in a special partnership *ipso facto* retains powers over the subject matter of the gift sufficient to make him taxable upon the income

thereof. Indeed, in *Nicholas v. Davis, supra,* the capital invested by the limited partners was given them by the general partners with the express understanding that such capital would be invested in the limited partnership; yet, the Court of Appeals for the Tenth Circuit held the partnership to be bona fide for tax purposes.

4. ". . . The taxpayer-settlor, on the other hand, retained complete control over the trust property which he had purportedly given away. . . ." (Brief 21) Here again, the Commissioner confuses the Taxpayer and the special partnership. Far from retaining complete control over the trust property, the Taxpayer divested himself of all interest therein and of all control excepting only such control as he could lawfully exercise in discharge of his duty of absolute good faith to his partners. *Watumull v. Ettinger, supra;* see *Toor v. Westover, supra.* As has been pointed out, retained powers of control over trust property, if they are to render the income therefrom taxable to the donor, must be exercisable by the donor in a non-fiduciary capacity.

5. ". . . He [the Taxpayer] was assured that it would immediately be returned for use in the business which he controlled. . . ." (Brief 21) Assurance that the trust corpus would be invested in a given business appears to be irrelevant under the *Clifford* doctrine unless that business is, in fact, controlled by the Taxpayer. And as has been so often repeated, the business of Edward D. Sultan Co. was controlled

by the Taxpayer only in his capacity as a fiduciary under a duty of absolute good faith to his fellow partners. Indeed, if this and the preceding proposition support the Commissioner's contention, then no transfer in trust wherein the donor named himself trustee could ever be sufficient to shift the incidence of taxation on the income of the transferred property, for in every such case the donor, as donee-trustee, would retain full control of the property (subject, of course, to the terms of the trust instrument) in his fiduciary capacity as trustee.

6. ". . . The partnership which he [the Taxpayer] dominated could also use it in any other business. . . ." (Brief 21-22) As has already been demonstrated, this statement is not in accord with the facts. The partnership was not "dominated" by the Taxpayer except as the general partner having the majority interest therein and, as such, the Taxpayer was bound to discharge a duty of absolute good faith to his fellow partners. Moreover, the partnership could not use the trust property "in any other business" except to the extent that the partnership engaged in another business. And if the partnership engaged in a business other than the wholesale jewelry business, it could do so only on behalf of and for the account of the respective partners, each of whom would share in the fruits of the enterprise in accordance with his capital contribution.

7. ". . . Its [the trust property's] use was to be without restriction by the donee-trust—because the

donee-trust was only a special or limited partner. . . ." (Brief 22) This statement merely recasts the statements numbered 2 and 4, *supra,* and is no more in accord with the facts or law than are those statements.

8. ". . . Its [the trust property's] continued availability was assured because the donee-trust was not free to withdraw or transfer its interest. . . ." (Brief 22) This statement is a mere repetition of the statement numbered 3, *supra.*

9. ". . . The other general partners were the taxpayer's own brothers and sister who also owed their interest to gifts from the taxpayer. . . ." (Brief 22) Although under *Helvering v. Clifford* the close family relationship is relevant, it is by no means controlling and, absent the retained powers of control and disposition emphasized by the Supreme Court, it becomes wholly immaterial. It is perhaps not without significance that the Commissioner does not challenge the status of Taxpayer's brothers and sister as partners in Edward D. Sultan Co.

10. ". . . He [the Taxpayer] could at any time buy out any of the others at book value plus their share of undistributed profits. . . ." (Brief 22) As pointed out above (p. 32), this statement is without support in any of the evidence in the record and is not in accord with the facts.

11. ". . . He [the Taxpayer] could continue the partnership indefinitely and it could likewise be continued by his personal representative upon his death.

. . . " (Brief 22) The power to refrain from exercising the option to terminate the partnership, whether vested in the Taxpayer or, after his death, in his personal representative, would only be relevant if one or more indicia of beneficial control of the trust property in the Taxpayer could be found. As has been demonstrated, however, all of the rights, powers and privileges of the Taxpayer under the trust deed and the special partnership agreement were exercisable by him only as a fiduciary owing a duty of absolute good faith to his fellow partners.

12. ". . . Determinations of the taxpayer, as owner of the majority in interest of the capital contributed by the general partners, were binding upon the partnership and he established the policy of the partnership. . . ." (Brief 22) As has been repeatedly reiterated, any determination by the Taxpayer, as owner of the majority in interest of the capital contributed by the general partners, could lawfully be made only in absolute good faith and in the interests and for the benefit of the partnership. No such determination could lawfully be made by the Taxpayer for his own personal benefit. It is far from uncommon for partnerships, general, special or limited, to utilize managing partners, and the practice has been given express recognition by the courts. *J. A. Riggs Tractor Co.,* 6 TC 889 (1946); *George Brothers & Co.,* 41 BTA 287 (1940).

Clearly, the powers held by the Taxpayer under the trust deed and partnership agreement—and he

held very few, if any, of those attributed to him by the Commissioner—do not singly or in the aggregate constitute the "bundle of rights" requisite for the invocation of the doctrine of *Helvering v. Clifford.*

The Commissioner, in his reliance on *Toor v. Westover, supra,* seeks to narrow the holding of this court to a degree unwarranted by the facts and the opinion therein.

That case originated as an action in the District Court for the Southern District of California against a collector of internal revenue to recover sums paid as a result of deficiency assessments of income tax. The case was tried, argued and submitted, and the District Court made and entered its findings of fact. These findings revealed the following situation: Plaintiff made trust agreements with a bank for the benefit of his children, and the trustee of the trusts so created executed articles of limited partnership with plaintiff as the general partner. Under the trust agreements the trustee was restricted to investments either in businesses in which plaintiff was a partner or principal shareholder, or in government bonds. The trust agreements were revocable by the plaintiff as grantor. Plaintiff retained exclusive dominion of the property, the disposition and allocation of the funds derived from the partnership business and all matters requiring judgment or management.

In no instance did the bank use its independent judgment on partnership matters nor did it exercise

any of the rights of partnership even by way of advice. The bank, as limited partner, did not exercise dominion and control over the trust corpus in the business nor did it influence the conduct of the partnership or the disposition of the income thereof. The partnership articles conferred on the plaintiff the absolute right to purchase the interest of the limited partner at its book value. There was no business purpose underlying the creation of the partnership, and the District Court commented that the conclusion was warranted that its sole object was to diminish tax liability.

The District Court, applying the *Tower*,[6] *Lusthaus*[7] and *Culbertson*[8] rules, found as a matter of fact that the plaintiff and the trustee-bank did not in good faith intend to join together in the present conduct of the business enterprise (94 F.Supp. 860, 864-66) and entered judgment for defendant.

On appeal to this court, the judgment of the District Court was affirmed in an opinion by Circuit Judge Orr. This court held that the donee trust did not become the substantial owner of a partnership interest which would entitle the partnership to recognition for tax purposes. In reaching that conclusion this court stated that considering the fact that the donee was neither free to remain out of the partner-

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[6]*Commissioner of Int. Rev. v. Tower,* 327 U.S. 280, 90 L.ed 670 (1946).

[7]*Lusthaus v. Commissioner of Int. Rev.,* 327 U.S. 293, 90 L.ed 679 (1946).

[8]*Commissioner v. Culbertson, supra.*

ship nor free to terminate or transfer its interest once the partnership was created, and that the plaintiff, as general manager, retained the powers of management and full discretion as to time and amounts of distribution of profits, the plaintiff remained the substantial owner of the interest he purported to have given away.

In its statement of the case this court recounted substantially all of the facts hereinabove referred to. It quoted the reports of the Senate and House Committees on the Revenue Bill of 1951[9] and in particular the statement that:

> "Substantial powers may be retained by the transferor as a managing partner or in any other fiduciary capacity which, when considered in the lights [sic] of all the circumstances, will not indicate any lack of true ownership in the transferee. In weighing the effect of a retention of any power upon the bona fides of a purported gift or sale, a power exercisable for the benefit of others must be distinguished from a power vested in the transferor for his own benefit."

saying of this statement:

> "We believe that this has always been the law." (200 F.2d 713, 716)

Thus it appears that in arriving at its decision in *Toor v. Westover, supra,* this court, while pointing out for the guidance of the lower court the significance of the fact that the donee-trust was neither

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[9]Sen. Rep. No. 781, 82d Cong. 1st Sess. (1951); H. R. Rep. No. 586, 82d Cong. 1st Sess. (1951).

free to remain out of the partnership nor to terminate or transfer its interest once the partnership was created, did not intend to rule that those facts alone and without regard to the other factors present—the revocability of the trust, the plaintiff's exclusive domination of the property and disposition of the funds derived from the partnership, the special partner's completely passive role, and the plaintiff's absolute right to buy out the limited partner at book value—were sufficient in themselves to establish retained substantial ownership in the purported donor.

To adopt the reading of *Toor v. Westover, supra,* contended for by the Commissioner, is to impute to this court a departure from the doctrine of both the *Culbertson* and the *Clifford* cases. The Supreme Court, in the *Culbertson* case, stressed the importance of considering all of the facts in any family partnership case, rather than attempting to apply one or two "objective" tests. And in the *Clifford* case, that court emphasized the cumulative effect of the entire bundle of rights retained by the purported donor, and held that they amounted in the aggregate to substantial ownership.

The Commissioner, however, urges that the holding of this court in the *Toor* case sets up two objective tests in family partnership cases, namely, that in order to be a bona fide partner, recognizable for income tax purposes, a partner must be (1) free to remain out of the partnership and (2) absolutely free to terminate or transfer his interest once the partner-

ship is created. Not only does this reading of the *Toor* case depart from the rationale of the *Culbertson* and *Clifford* cases, but it also tends to bring this court into unnecessary conflict with the Courts of Appeals for the Eighth and Tenth Circuits. *Thompson v. Riggs,* 175 F.2d 81 (8th Cir. 1949); *Nicholas v. Davis,* 204 F.2d 200 (10th Cir. 1953).

Thompson v. Riggs, supra, was an appeal from a judgment for the plaintiff in an action for refund of income taxes. The plaintiff was the owner of a 60% interest in a partnership in which the remaining 40% interest belonged to his son. Plaintiff transferred out of his 60% interest, 5% each to six irrevocable trusts for the benefit of plaintiff's wife and plaintiff's son's family. Plaintiff, his son and a bank were named trustees of each of the trusts. Plaintiff, his son and the trustees then entered into a new partnership agreement.

The trust instruments provided in relevant part that on all matters concerning the management and control of the partnership business, authority to speak for the trustees was vested in plaintiff and his son to the exclusion of the bank, and that the bank was to act as a naked trustee exercising no discretion and being charged with no liability or responsibility for or arising out of the conduct of the partnership business. The trustees could withdraw from the partnership, but any decision as to whether to do so was to be made solely by the plaintiff and his son to the exclusion of the bank. Similarly, the trus-

tees could acquire additional interests in the partnership, but the right to determine whether to do so was vested solely in the plaintiff and his son.

The partnership agreement provided that the management of the partnership business was vested in the plaintiff and his son (and plaintiff's grandson when and if he attained maturity and so long as he retained an interest in the business either as trustee or individually), and further provided that in the event of any disagreement as to the management of the partnership business, the decision of the plaintiff would control so long as he retained an interest in the business individually or as trustee. No partner could assign his interest (except to another partner) without the consent of all of the partners. The trust for the benefit of plaintiff's grandson had an option to purchase the interest of any of the other trusts at net book value.

Since the transfer was of an interest in the partnership and since the right to determine whether any trust should withdraw from the partnership was retained by the plaintiff and his son, the trusts were not free to remain out of the partnership. Since no partner could transfer his interest without the consent of all of the partners (including the plaintiff), none of the trusts was absolutely free to transfer its interest once the partnership was created. Nevertheless, the Court of Appeals, reviewing all of the facts and with the case of *Helvering v. Clifford* having been called to its attention, affirmed the judgment for the plaintiff.

Nicholas v. Davis, supra, concerned three successive partnership, the second of which was a limited partnership. In the second partnership the limited partners were the wives of the general partners. Each general partner gave to his wife certain sums of money from the capital assets of the preceding partnership, with the understanding among all of them that the gifts were to be used for the purchase of limited partners' interests in the second partnership. It appears that the limited partners could neither withdraw nor transfer their interests, since the limited partnership agreement provided that it was to continue for a stated term and that the limited partners would be entitled to the return of their contributions upon the expiration of the term of the partnership, upon the dissolution of the partnership, or upon the consent of all of the other members of the partnership, both general and limited.

The Commissioner assessed a deficiency in income tax against one of the general partners on the thory that the income of his wife as a limited partner was in reality income of that general partner. The general partner concerned brought an action against a collector to recover the amount of the deficiency assessment paid, and the cause was tried before a jury. The plaintiff offered evidence showing, among other things, the facts set out above and the fact that the limited partner enjoyed complete dominion over her distributive share of partnership income, and the collector offered no evidence whatever. By direction of the trial court, a verdict was returned in favor of the

plaintiff taxpayer. On appeal from a judgment entered thereon, the Court of Appeals for the Tenth Circuit affirmed the judgment, holding that no question of credibility or issue of fact was presented for determination by a jury.

In each of the foregoing cases the challenged partner was not absolutely free to remain out of the partnership or to terminate or transfer his interest once the partnership was created. On all of the facts in the record, however, those courts held the partnerships concerned to be bona fide recognizable partnerships for income tax purposes.

Given a case in which an examination of all of the evidence leaves doubt as to whether in fact and in law the donor of property has retained such control and dominion thereof as to render him liable for taxes on the income thereof under the doctrine of the *Clifford* case, the addition of the two factors mentioned could properly be sufficient to turn the decision in favor of taxability. It is respectfully submitted that such was the case in *Toor v. Westover, supra,* and that this court, in arriving at its decision in that case, did not base its determination solely upon these two factors, but rather, considering all of the circumstances, found a lack of true ownership in the transferee of the trust property. This rationale is not only borne out by this court's opinion, but also avoids the creation of a conflict of decision between this and the Eighth and Tenth Circuits.

CONCLUSION.

For the reasons set forth, the decisions of the Tax Court are correct and should be affirmed.

Dated, Honolulu, Hawaii,
November 2, 1953.

Respectfully submitted,
MILTON CADES,
Attorney for Respondents.

SMITH, WILD, BEEBE & CADES,
Of Counsel.

(Appendix Follows.)

Appendix.

Appendix

Internal Revenue Code:

Sec. 22. Gross Income

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, business, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U.S.C. 1946 ed., Sec. 22.)

Sec. 182. Tax of Partners.

In computing the net income of each partner, he shall include, whether or not distribution is made to him——

* * * * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

(26 U.S.C. 1946 ed., Sec. 182.)

Revised Laws of Hawaii (1935):

Chapter 225. Partnerships, Registration of.

* * * * * * *

Part 2. Special

Sec. 6870. *Between individuals.*—A partnership may be formed between two or more individuals for the transaction of any lawful business. A special partnership may be formed between one or more persons, called general partners, and one or more persons called special partners, for the transaction of any business.

* * * * * * *

Sec. 6880. *Only general partners act.*—The general partners only shall have authority to transact the business of a special partnership.

Sec. 6881. *Special partners may advise.*—A special partner may at all times investigate the partnership affairs and advise his partners or their agents as to their management.

Sec. 6882. *May loan money. Insolvency.*—A special partner may lend money to the partnership or advance money for it, or to it, and take from it security therefor, and as to such secured loans or advances has the same rights as any other creditor, but in case of the insolvency of the partnership all other claim which he may have against it must be postponed until all other creditors are satisfied.

Sec. 6883. *Receive interest and profits.*—A special partner may receive such lawful interest and such

proportion of profits as may be agreed upon, if not paid out of the capital invested in the partnership by him or some other special partner, and is not bound to refund the same to meet subsequent losses.

Sec. 6884. *May not withdraw capital.*—No special partner, under any pretense, may withdraw any part of the capital invested by him in the partnership during its continuance.

Sec. 6885. *Result of withdrawing capital.*—If a special partner withdraws capital from the firm, contrary to the provisions of sections 6883 or 6884, he thereby becomes a general partner.

* * * * * * *

LIABILITY OF PARTNERS.

* * * * * * *

Sec. 6887. *Of special partners.*—The contribution of a special partner to the capital of the firm, and the increase thereof, is liable for its debts; but he is not otherwise liable therefor, except as follows:

1. If he has wilfully made or permitted a false or materially defective statement in the certificate of the partnership, the affidavit filed therewith, or the published announcement thereof, he is liable as a general partner to all creditors of the firm; or,

2. If he has wilfully interfered with the business of the firm, except as permitted hereinabove, he is liable in like manner; or,

3. If he has wilfully joined in or assented to an act contrary to any of the provisions of sections 6880-6885, he is liable in like manner.

Sec. 6888. *For unintentional act.*—When a special partner has, unintentionally, done any of the acts mentioned in the last section, he is liable, as a general partner, to any creditor of the firm who has been actually misled thereby to his prejudice.

No. 13805

United States
Court of Appeals
for the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD,
Respondents.

Transcript of Record

Petition to Review Decisions of The Tax Court of the United States

FILED
JUL 23 1953
PAUL P. O'BRIEN
CLERK

Phillips & Van Orden Co., 870 Brannan Street, San Francisco, Calif.

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INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

APPEARANCES

For Petitioners:

MILTON CADES, Esq.,
URBAN E. WILD, Esq.

For Respondent:

CHARLES W. NYQUIST, Esq.

Docket No. 29391

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DOCKET ENTRIES

1950

July 3—Petition received and filed. Taxpayer notified. Fee paid.

July 3—Request for Circuit hearing in Honolulu, T. H., filed by taxpayer. 7/17/50 Granted.

July 3—Notice of appearance of Milton Cades, Esq., and Urban E. Wild, Esq., as Counsel, filed. Copy served.

July 5—Copy of Petition served on General Counsel.

Aug. 8—Answer filed by General Counsel.

1950

Aug. 10.—Copy of Answer served on taxpayer. Honolulu, T. H.

1951

Mar. 12—Hearing set June 13, 1951, Honolulu, T.H.

May 22—Hearing changed to June 15, 1951, Honolulu, T. H.

June 20—Hearing had before Judge Arundell on merits. Proceedings consolidated for hearing. Stipulation of facts, with exhibits 1 through 45, filed. Petitioner's brief, August 29, 1951. Respondent's brief, October 15, 1951. Petitioner's reply, November 29, 1951.

June 27—Hearing had before Judge Arundell. Proceedings reopened to receive additional exhibits on behalf of respondent.

July 18—Transcript of Hearing, 6/20/51 filed.

Aug. 27—Brief filed by taxpayer. 8/28/51 Copy served.

Oct. 15—Reply Brief filed by General Counsel. Copy served.

Oct. 22—Motion for extension to January 28, 1952, to file reply brief, filed by taxpayer. 10/23/51—Granted.

1952

Jan. 31—Reply brief filed by taxpayer. Copy served.

July 7—Findings of fact and opinion rendered. Judge Arundell. Decision will be entered under Rule 50. Copy served.

Oct. 9—Respondent's computation for entry of decision filed.

1952

Oct. 19—Hearing set November 19, 1952, at Washington, D. C., on respondent's computation.

Oct. 30—Consent to settlement filed by taxpayer.

Oct. 31—Decision entered. Judge Arundell. Div. 7.

1953

Jan. 19—Petition for Review by U. S. Court of Appeals for the Ninth Circuit, filed by General Counsel.

Feb. 6—Proofs of Service on Counsel and Taxpayers filed.

Feb. 12—Motion for extension of time to 4/17/53 to transmit record, filed by General Counsel.

Feb. 13—Order extending time to 4/17/53 to prepare, transmit and deliver record, entered.

April 2—Statement of Points filed by General Counsel, with statement of service thereon.

April 2—Statement Re Diminution of Record filed by General Counsel, with statement of Service thereon.

Docket No. 29392

[Printer's Note: Appearances, Title of Cause and Docket Entries are duplicates of Docket No. 29391 except June 20, 1951, which is as follows:]

June 20—Hearing had before Judge Arundell on merits. Proceedings consolidated for hearing. Respondent's motion for leave to file amendment to answer—granted. Amendment to Answer and Reply to amendment to answer filed and served. Stipulation of facts, with Exhibits 1 through 45, filed. Petitioner's brief, August 29, 1951. Respondent's brief, October 15, 1951. Petitioner's reply, November 29, 1951.

The Tax Court of the United States

Docket No. 29391

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency, Bureau symbols IT:FC:LMJ-150D, dated February 7, 1950, and, as a basis of their proceeding, allege as follows:

I.

The petitioners are individuals whose mailing ad-

dress is 843 Kaahumanu Street, Honolulu, T. H. The returns here involved were filed with the Collector for the Honolulu Division.

II.

The notice of deficiency, a copy of which is attached and marked "Exhibit A", was mailed to the petitioners on February 7, 1950.

III.

The taxes in controversy are income taxes for the calendar year 1948. The deficiency asserted is $1,177.22, the entire amount of which is in controversy.

IV.

The determination of tax set forth in said notice of deficiency is based on the following errors:

1. The Commissioner of Internal Revenue has erred in the determination that the special partnership of Ace Distributors, formerly known as T. H. Brodhead Company, formed under partnership agreement, dated September 30, 1942, as amended on February 28, 1943, and February 28, 1947, composed of Thomas H. Brodhead as a general partner, and the Elizabeth S. Brodhead Trust as a special partner, is not a valid partnership for income tax purposes, and that all income of the said partnership of Ace Distributors for the taxable year 1948 is taxable to the petitioners.

2. The Commissioner of Internal Revenue has erred in determining that the income from the partnership of Ace Distributors, reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust for the taxable year 1948, is eliminated from such fiduciary return and is taxable to the petitioners.

3. The Commissioner of Internal Revenue has erred in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1948 by adding thereto the sum of $20,177.91, being the portion of a net capital gain from the sale of land and buildings made by the partnership of Ace Distributors (and reported on the partnership return for the fiscal year ended February 28, 1949) constituting income of the Elizabeth S. Brodhead Trust and returned by it for tax purposes and the tax thereon having been paid by said Trust.

4. The Commissioner of Internal Revenue has erred in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1948 by decreasing the business income of petitioners for said year by the amount of $16,009.79 arrived at by attributing to petitioners that portion of the losses of Ace Distributors constituting losses of the Elizabeth S. Brodhead Trust and returned by it for tax purposes and used in the computation of the tax liability of said Trust.

5. The Commissioner of Internal Revenue has erred in determining that the income tax liability for the petitioners is $4,062.80 for the taxable year ended December 31, 1948.

6. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $1,177.22 or of any part thereof in petitioners' income tax for the taxable year ended December 31, 1948.

V.

The facts upon which the petitioners rely as the basis for this proceeding are as follows:

1. The petitioner, Elizabeth S. Brodhead, on February 28, 1943, settled the Elizabeth S. Brodhead Trust by a transfer to the Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, and to Mortimer J. Glueck, a resident of the Territory of Hawaii, as Trustees, of the sum of $10,000.00 under the hereinafter-mentioned terms and conditions.

2. By the terms of the Elizabeth S. Brodhead Trust Agreement, the interest of the Thomas H. Brodhead Trust as a special partner in the partnership of T. H. Brodhead Company was to be purchased by the said Elizabeth S. Brodhead Trust, the income from which interest was to be accumulated until the beneficiaries, the children of the petitioners, reached the age of twenty-three, at which time the Trust was to be terminated, and the corpus and accumulated income was to be distributed to the beneficiaries.

3. By the terms of the Elizabeth S. Brodhead Trust, the petitioner, Elizabeth S. Brodhead, completely divested herself of all right, title or interest in the Trust Estate, both corpus and income, the same being at all times held by the Trustees, to wit, the Bishop Trust Company, Limited, and Mortimer J. Glueck who is unrelated by blood or marriage to the petitioner, Elizabeth S. Brodhead.

4. By the terms of the Elizabeth S. Brodhead Trust, Elizabeth S. Brodhead has no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever, such right of disposition being confined to the terms of the Trust instrument, and to be exercised, where permissible under the terms of the Trust, within the sole direction of the Trustees.

5. By the terms of the Elizabeth S. Brodhead Trust, Thomas H. Brodhead, one of the petitioners herein, has no interest in the Elizabeth S. Brodhead Trust and has no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever.

6. On September 30, 1942, the petitioner, Thomas H. Brodhead, and the Thomas H. Brodhead Trust entered into an agreement of special partnership in accordance with and under the laws of the Territory of Hawaii, by which agreement the petitioner, Thomas H. Brodhead, became a general partner, and the Thomas H. Brodhead Trust became a special partner in the partnership of T. H. Brodhead Company.

7. On February 28, 1943, the special partnership agreement between the petitioner, Thomas H. Brodhead, and the Thomas H. Brodhead Trust was amended in accordance with the laws of the Territory of Hawaii. By virtue of the amendment, the Thomas H. Brodhead Trust withdrew as a special

partner, and the Elizabeth S. Brodhead Trust was admitted as a special partner in the special partnership of T. H. Brodhead Company, which partnership was in conformity with the laws of the Territory of Hawaii and was a bona fide and valid partnership for all purposes.

8. On February 28, 1947, the special partnership agreement between Thomas H. Brodhead and the Elizabeth S. Brodhead Trust was amended in accordance with the laws of the Territory of Hawaii, by virtue of which amendment the special partnership composed of Thomas H. Brodhead as general partner, and the Elizabeth S. Brodhead Trust as special partner, changed the partnership name from the T. H. Brodhead Company to Ace Distributors.

9. The Elizabeth S. Brodhead Trust for the fiscal year ended September 30, 1948, filed a return in which was computed the amount of $5,487.84 as its loss from its interest in the partnership of Ace Distributors, the loss so computed being properly computed on the said income tax return of the said Elizabeth S. Brodhead Trust.

10. The gross income of the Elizabeth S. Brodhead Trust for the fiscal year ended September 30, 1949, included income from the partnership of Ace Distributors in the amount of $2,110.47, computed on the basis of a loss from its interest in the partnership of Ace Distributors in the amount of $7,978.48 and a long term capital gain of $10,088.98, being its share of the capital gain of the Ace Dis-

tributors, all of which items were properly computed by the Elizabeth S. Brodhead Trust, and the net income of $2,110.47 was properly returned by said Elizabeth S. Brodhead Trust for the fiscal year ended September 30, 1949, the income tax being computed thereon, and the tax thereon being properly paid by the said Elizabeth S. Brodhead Trust.

Wherefore, the petitioners pray that this Court may hear the proceeding and determine that there is no deficiency due from the petitioners for the year 1948.

/s/ THOMAS H. BRODHEAD
/s/ ELIZABETH S. BRODHEAD
843 Kaahumanu Street,
Honolulu, T. H.

Territory of Hawaii,
City and County of Honolulu—ss.

Thomas H. Brodhead and Elizabeth S. Brodhead, being duly sworn, say that they are the petitioners above-named; that they have read the foregoing petition, or had the same read to them, and are familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and that those they believe to be true.

/s/ THOMAS H. BRODHEAD
/s/ ELIZABETH S. BRODHEAD

Subscribed and sworn to before me this 30th day of June, 1950.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires 6-30-53.

EXHIBIT A

Form 1230 SN-IT-1

IT:FC:LMJ-150D Feb. 7, 1950

Mr. Thomas H. Brodhead and Mrs. Elizabeth S. Brodhead, Husband and Wife,
843 Kaahumanu Street, Honolulu, T. H.

Dear Sir and Madam:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1948 discloses a deficiency of $1,177.22 as shown in the attached statement.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 150 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 150th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D.C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P.O. Box 421, Honolulu 9, T.H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner

/s/ By H. A. PETERSON,
Internal Revenue Agent in Charge

Enclosures: Statement, Form 1276, Form of Waiver

STATEMENT

Year	Deficiency
1948	$1,177.22

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated July 22, 1949 and to your protest dated October 3, 1949.

A copy of this letter and statement has been mailed to your representatives, Cameron & John-

stone, P.O. Box 2906, Honolulu 2, T.H., in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1948

Adjustments to Net Income

Net income as disclosed by return	$17,015.08
Unallowable deductions and additional income:	
(a) Net capital gains	20,177.91
Total	$37,192.99
Nontaxable income and additional deductions:	
(b) Business income decreased	16,009.79
Net income adjusted	$21,183.20

Explanation of Adjustments

(a) It has been determined that Ace Distributors (formerly T. H. Brodhead Company) an alleged partnership between Thomas H. Brodhead and the Elizabeth S. Brodhead Trust, is not a valid partnership for Federal income tax purposes, and that all income from Ace Distributors (formerly T. H. Brodhead Company) is taxable to you, with the result that the income or loss from Ace Distributors (formerly T. H. Brodhead Company) reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust is eliminated from such fiduciary return.

In view of this determination, the income or loss from Ace Distributors (formerly T. H. Brodhead Company) which you reported on a fiscal year basis in line with the fiscal year basis used by the alleged partnership, must be adjusted to the calendar year basis used on your individual income tax returns. Accordingly, a portion of the income or loss reported by the alleged partnership, Ace Distributors (formerly T. H. Brodhead Company) for the fiscal year 3/1/47 to 2/29/48, and a portion of the income or loss reported by the alleged partnership, Ace Distributors (formerly T. H. Brodhead Company) for the fiscal year 3/1/48 to 2/28/49, is allocated to the calendar year 1948, based on the respective number of days in 1948, as computed in item (b) below.

The net capital gain of $20,177.91 from the sale of land and buildings, Kawaiaho Court, acquired in 1944 and sold in 1948, which was reported on the partnership return of the alleged partnership, Ace Distributors (formerly T. H. Brodhead Company) for the fiscal year ending 2/28/49, is not subject to an allocation and is held to be taxable to you in 1948 when the sale took place.

(b) The computation of your revised business income or loss from the alleged partnership, Ace Distributors (formerly T. H. Brodhead Company) for the calendar year 1948 is as follows:

Ordinary net loss reported on partnership return for the fiscal year 3-1-47 to 2-29-48	$ 5,487.84
Less: Prepaid insurance erroneously written off	143.80
Ordinary net loss for fiscal year 3-1-47 to 2-29-48 revised	$ 5,344.04
Ordinary net loss reported on partnership return for the fiscal year 3-1-48 to 2-28-49—not changed	$15,956.99
Pro-rata portion of $5,344.04 applicable to calendar year ending 12-31-48 (1-1-48 to 2-29-48): 60/366 of $5,344.04	$ 876.07
Pro-rata portion of $15,956.99 applicable to calendar year ending 12-31-48 (3-1-48 to 12-31-48): 306/365 of $15,956.99	19,377.64
to 12-31-48): 306/365 of $15,956.99	13,377.64
Revised business loss from Ace Distributors (formerly T. H. Brodhead Co.) for calendar year 1948	$14,253.71
Business income from above sources reported on your 1948 return	1,756.08
Business income decreased for the calendar year 1948	$16,009.79

Computation of Tax

Net income adjusted		$21,183.20
Less: Exemptions		3,000.00
Income subject to tax		$18,183.20
One-half of $18,183.20		$ 9,091.60
Tentative income tax on $9,091.60	$2,331.14	
Less: Reduction	299.74	
Difference	$2,031.40	
Correct income tax liability ($2,031.40x2)		$ 4,062.80
Income tax liability disclosed by return, Account No. 301881		2,885.58
Deficiency in income tax		$ 1,177.22

[Endorsed]: T.C.U.S. Filed July 3, 1950.

[Title of Tax Court and Cause No. 29391.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioners admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the petition.

IV and IV-1 to 6, inclusive. Denies that the Com-

missioner erred in the determination of the deficiency as alleged in paragraph IV of the petition and subparagraphs 1 to 6, inclusive, thereunder.

V-1 to 10, inclusive. Denies the allegations contained in subparagraphs 1 to 10, inclusive, of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioners' appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue

Of Counsel:

B. H. NEBLETT,
Division Counsel;
T. M. MATHER,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Aug. 8, 1950.

The Tax Court of the United States

Docket No. 29392

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency, Bureau symbols IT:FC:LMJ-150D, dated February 7, 1950, and, as a basis of their proceeding, allege as follows:

I.

The petitioners are individuals whose mailing address is 843 Kaahumanu Street, Honolulu, T. H. The returns here involved were filed with the Collector for the Honolulu Division.

II.

The notice of deficiency, a copy of which is attached and marked "Exhibit A", was mailed to the petitioners on February 7, 1950.

III.

The taxes in controversy are income taxes for the calendar years 1943 to 1945, inclusive. The deficiency asserted is $170,891.90, the entire amount of which is in controversy.

IV.

The determination of tax set forth in said notice of deficiency is based on the following errors:

1. The Commissioner of Internal Revenue has erred in including in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1942 the sum of $40,624.38 as income to the petitioners, rather than as income for the taxable year ended December 31, 1943 to the petitioner, Thomas H. Brodhead, and to the Thomas H. Brodhead Trust as partners in the partnership of T. H. Brodhead Company, a special partnership organized and doing business under the laws of the Territory of Hawaii for the fiscal period October 1, 1942 to February 28, 1943.

2. The Commissioner of Internal Revenue has erred in the determination that the special partnership of T. H. Brodhead Company, formed under Partnership Agreement dated September 30, 1942 with petitioner, Thomas H. Brodhead as a general partner and the Thomas H. Brodhead Trust as a special partner, as well as the partnership of T. H. Brodhead Company as changed on February 28, 1943 by the withdrawal of the Thomas H. Brodhead Trust as a special partner and the admission of the Elizabeth S. Brodhead Trust as a special partner, is not a valid partnership for income tax purposes, and that all income of the original and amended T. H. Brodhead Company for the taxable years 1942 through 1946 is taxable to the petitioners.

3. The Commissioner of Internal Revenue has

erred in allowing in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1942 an additional deduction in the amount of $13.40 for contributions made by the partnership of T. H. Brodhead Company.

4. The Commissioner of Internal Revenue has erred in determining that the income tax liability for the petitioners is $85,704.06 for the taxable year ended December 31, 1942.

5. The Commissioner of Internal Revenue has erred in determining that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust for the taxable year 1943 is eliminated from such fiduciary return and is taxable to the petitioners.

6. The Commissioner of Internal Revenue has erred in including in the determination of the petitioners' income tax net income and victory tax net income for the taxable year ended December 31, 1943 the sum of $33,449.51, being an allocation of income during the year 1943 of the Elizabeth S. Brodhead Trust from its interest in the T. H. Brodhead Company, a special partnership.

7. The Commissioner of Internal Revenue has erred in disallowing in the determination of petitioners' income tax net income and victory tax net income from the partnership of T. H. Brodhead Company a deduction of $100.00 for legal fees incurred and paid by the T. H. Brodhead Company during the year ended December 31, 1943.

8. The Commissioner of Internal Revenue has erred in allowing in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1943 an additional deduction in the amount of $585.64 for contributions made by the partnership of T. H. Brodhead Company.

9. The Commissioner of Internal Revenue has erred in determining that the amount of income and victory tax liability for the petitioners for the year 1943 which is unforgiven in the taxable year ended December 31, 1943 is $18,301.43.

10. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $42,280.89 or of any part thereof in petitioners' income and victory tax for the taxable year ended December 31, 1943.

11. The Commissioner of Internal Revenue has erred in determining that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust for the taxable year 1944 is eliminated from such fiduciary return and is taxable to the petitioners.

12. The Commissioner of Internal Revenue has erred in including in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1944 the sum of $95,106.88, representing income received by the Elizabeth S. Brodhead Trust during the calendar year 1944 from its interest in the T. H. Brodhead Company, a special partnership.

13. The Commissioner of Internal Revenue has erred in allowing in the determination of the petitioners' income tax net income for the taxable year ended December 31, 1944 an additional deduction in the amount of $4,250.50 for contributions made by the partnership of T. H. Brodhead Company.

14. The Commissioner of Internal Revenue has erred in determining that the income tax liability for the petitioners is $110,299.10 for the taxable year ended December 31, 1944.

15. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $79,944.90 or of any part thereof in petitioners' income tax for the taxable year ended December 31, 1944.

16. The Commissioner of Internal Revenue has erred in determining that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust for the taxable year 1945 is eliminated from such fiduciary return and is taxable to the petitioners.

17. The Commissioner of Internal Revenue has erred in including in the determination of petitioners' income tax net income for the taxable year ended December 31, 1945 the sum of $55,690.75, representing income to the Elizabeth S. Brodhead Trust from its interest in the T. H. Brodhead Company, a special partnership.

18. The Commissioner of Internal Revenue has erred in allowing in the determination of the petitioners' income tax net income for the taxable year

ended December 31, 1945 an additional deduction in the amount of $1,395.11 for contributions made by the partnership of T. H. Brodhead Company during its fiscal year March 1, 1944 to February 28, 1945 and from March 1, 1945 to February 28, 1946, as allocated to the calendar year 1945.

19. The Commissioner of Internal Revenue has erred in determining that the income tax liability for the petitioners is $100,198.87 for the taxable year ended December 31, 1945.

20. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $48,666.11 or of any part thereof in petitioners' income tax for the taxable year ended December 31, 1945.

V.

The facts upon which the petitioners rely as the basis for this proceeding are as follows:

1. The statute of limitations bars the Commissioner of Internal Revenue from asserting a deficiency in tax for the year 1943, the tax return for said year having been filed not later than March 15, 1944, and no extension of time for the assessment of said tax having been executed.

2. The petitioner, Thomas H. Brodhead, on September 30, 1942 settled the Thomas H. Brodhead Trust by a transfer to the Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, and to Mortimer J. Glueck, a resident of the Territory of Hawaii, as Trustees,

of the sum of $40,000.00 under the hereinafter-mentioned terms and conditions.

3. By the terms of the Thomas H. Brodhead Trust Agreement, a fifty percent (50%) interest in the T. H. Brodhead Company, a special partnership organized under the laws of the Territory of Hawaii, was to be purchased by the said Trust, the income from which interest was to be accumulated until the beneficiaries, the children of the petitioners, reached the age of twenty-one years, with discretion in the aforementioned Trustees to pay out of the net income of the Trust amounts necessary for the maintenance, support and education of the beneficiaries.

4. The special partnership of T. H. Brodhead Company was formed under Partnership Agreement dated September 30, 1942 in conformity with the laws of the Territory of Hawaii, and was a bona fide and valid partnership for all purposes.

5. By the terms of the Thomas H. Brodhead Trust, the petitioner, Thomas H. Brodhead, completely divested himself of all right, title or interest in the Trust Estate, both corpus and income, and has vested the same in the Trustees, to wit, the Bishop Trust Company, Limited, and Mortimer J. Glueck who is unrelated by blood or marriage to petitioner, Thomas H. Brodhead.

6. By the terms of the Thomas H. Brodhead Trust, Thomas H. Brodhead has no right or power, discretionary or otherwise, to make any distribution

of income or principal, current or accumulated, in any manner whatsoever, such right of disposition being confined to the terms of the Trust instrument and to be exercised, where permissible under the terms of the Trust, within the sole discretion of the Trustees.

7. By the terms of the Thomas H. Brodhead Trust, Elizabeth S. Brodhead, one of the petitioners herein, had no interest in the Thomas H. Brodhead Trust and had no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever.

8. The gross income of the Thomas H. Brodhead Trust for the fiscal year ended September 30, 1943 included income from the partnership of T. H. Brodhead company amounting to $34,319.30, all of which income was returned by said Thomas H. Brodhead Trust for the fiscal year ended September 30, 1943, the income tax being computed thereon, and the tax thereon being properly paid by the Thomas H. Brodhead Trust.

9. On February 28, 1943, petitioner, Thomas H. Brodhead, made a gift to his wife, Elizabeth S. Brodhead, and transferred to her cash in the amount of $10,000.00, which transfer he disclosed on his gift tax return filed for the year 1943, the gift tax being computed thereon, and the tax thereon being paid by petitioner, Thomas H. Brodhead.

10. The petitioner, Elizabeth S. Brodhead, on February 28, 1943 settled the Elizabeth S. Brod-

head Trust by a transfer to the Bishop Trust Company, Limited, and Mortimer J. Glueck, as Trustees, of the sum of $10,000.00 under the hereinafter-mentioned terms and conditions.

11. By the terms of the Elizabeth S. Brodhead Trust Agreement, the interest of the Thomas H. Brodhead Trust, as special partner in the partnership of T. H. Brodhead Company, was to be purchased by the said Elizabeth S. Brodhead Trust, the income from which interest was to be accumulated until the beneficiaries, the children of the petitioners, reached the age of twenty-three, at which time the Trust was to be terminated and the corpus and accumulated income to be distributed to the beneficiaries.

12. The T. H. Brodhead Company, in which the Elizabeth S. Brodhead Trust became a special partner, was formed under Partnership Agreement dated September 30, 1942, and amended on February 28, 1943, all in conformity with the laws of the Territory of Hawaii, and was and is a bona fide and valid partnership for all purposes.

13. By the terms of the Elizabeth S. Brodhead Trust, the petitioner, Elizabeth S. Brodhead, completely divested herself of all right, title or interest in the Trust Estate, both corpus and income, the same being at all times held by the Trustees, to wit, the Bishop Trust Company, Limited, and Mortimer J. Glueck who is unrelated by blood or marriage to the petitioner, Elizabeth S. Brodhead.

14. By the terms of the Elizabeth S. Brodhead

Trust, Elizabeth S. Brodhead has no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever, such right of disposition being confined to the terms of the Trust instrument, and to be exercised, where permissible under the terms of the Trust, within the sole direction of the Trustees.

15. By the terms of the Elizabeth S. Brodhead Trust, Thomas H. Brodhead, one of the petitioners herein, had no interest in the Elizabeth S. Brodhead Trust and had no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever.

16. The gross income of the Elizabeth S. Brodhead Trust for the taxable year 1944 included income from the partnership of T. H. Brodhead Company amounting to $40,895.44, all of which income was returned by said Elizabeth S. Brodhead Trust for the year 1944, the income tax being computed thereon and the tax thereon being properly paid by the said Elizabeth S. Brodhead Trust.

17. The gross income of the Elizabeth S. Brodhead Trust for the taxable year 1945 included income from the partnership of the T. H. Brodhead Company amounting to $67,914.53, all of which income was returned by said Elizabeth S. Brodhead Trust, the income tax on said income being properly paid by the said Elizabeth S. Brodhead Trust.

18. The additional contributions which the Commissioner of Internal Revenue has erred in allow-

ing as deductions to the petitioners were contributions which were, in fact, made by and were allowable to the partnership of T. H. Brodhead Company in the years 1942 through 1945.

19. During the fiscal period October 1, 1942 to February 28, 1943, legal services were rendered to the partnership of T. H. Brodhead Company in connection with the drafting of the special partnership agreement of that company, the bill for which services was rendered and paid by the partnership of T. H. Brodhead Company during the said fiscal period and was properly claimed as a deduction in the determination of the ordinary income of the partnership for the said period as an ordinary and necessary business expense. The Commissioner of Internal Revenue has erred in disallowing this contribution.

Wherefore, the petitioners pray that this Court may hear the proceeding and determine that there is no deficiency due from the petitioners for the years 1943, 1944 and 1945.

/s/ THOMAS H. BRODHEAD,
/s/ ELIZABETH S. BRODHEAD

Territory of Hawaii,
City and County of Honolulu—ss.

Thomas H. Brodhead and Elizabeth S. Brodhead, being duly sworn, say that they are the petitioners above-named; that they have read the foregoing petition, or had the same read to them, and are familiar with the statements contained therein, and

that the statements contained therein are true, except those stated to be upon information and belief, and that those they believe to be true.

/s/ THOMAS H. BRODHEAD
/s/ ELIZABETH S. BRODHEAD

Subscribed and sworn to before me this 30th day of June, 1950.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires 6-30-53.

EXHIBIT A

Form 1230 SN-IT-1

IT:FC:LMJ-150D Feb. 7, 1950

Mr. Thomas H. Brodhead and Mrs. Elizabeth S. Brodhead, Husband and Wife,
843 Kaahumanu Street, Honolulu, T. H.

Dear Sir and Madam:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1943, December 31, 1944, and December 31, 1945, discloses a deficiency of $170,891.90 as shown in the attached statement.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 150 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 150th day) from the date of the mailing of this

letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D.C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P.O. Box 421, Honolulu 9, T. H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner

/s/ By H. A. PETERSON,
Internal Revenue Agent in Charge

Enclosures: Statement, Form 1276, Form of waiver.

STATEMENT

Year	Deficiency
1943	$42,280.89
1944	79,944.90
1945	48,666.11
Total	$170,891.90

In making this determination of your income tax

liability, careful consideration has been given to the reports of examination dated December 29, 1947 and September 22, 1948, to your protests dated April 23, 1948 and November 26, 1948, and to statements made at a conference held on June 27, 1949.

A copy of this letter and statement has been mailed to your representatives, Cameron & Johnstone, P.O. Box 2906, Honolulu 2, T. H., in accordance with the authority contained in the power of attorney executed by you.

TAXABLE YEAR ENDED DECEMBER 31, 1942

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return	$ 85,260.02
Unallowable deductions and additional income:	
(a) Business income increased	40,624.38
Total	$125,884.40
Nontaxable income and additional deductions:	
(b) Contributions increased	13.40
Net income adjusted	$125,871.00

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that the T. H. Brodhead Company, an alleged partnership, is not a valid partnership for Federal income tax purposes and that all income from the T. H. Brodhead Company is taxable to you. In view of this determination, the income from the T. H. Brodhead Company, which you reported on a fiscal year basis in line with the fiscal year basis used by the alleged partnership, must be adjusted to the calendar year basis used on your individual income tax returns. Accordingly, a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the period October 1, 1942 to February 28, 1943, is allocated to the calendar year 1942 based on the number of days it was in existence in the year 1942. The computation of your revised business income from the alleged partnership, T. H. Brodhead Company, is as follows:

Ordinary net income reported on partnership return for the period 10-1-42 to 2-28-43		$ 79,741.63
Add: Gross income taxes overstated	$ 1,913.97	
Partnership filing fee erroneously charged to expense	1.00	1,914.97
Total		$ 81,656.60
Less: Excessive profits on contract sales to U. S. Government per renegotiation settlement	$ 12,000.00	
Additional gross income taxes not accrued on books	4,853.06	16,853.06
Ordinary net income for period 10-1-42 to 2-28-43 revised		$ 64,803.54
Pro-rata portion of $64,803.54 applicable to calendar year ending 12-31-43 (1-1-43 to 2-28-43) : 59/151 of $64,803.54		25,320.59
Pro-rata portion of $64,803.54 applicable to calendar year ending 12-31-42 (10-1-42 to 12-31-42) : 92/151 of $64,803.54, representing your revised business income from the alleged partnership, T. H. Brodhead Company, for the year 1942, not reported on your 1942 individual income tax return		$ 39,482.95
Add: Additional adjustments not applicable to the business income of the alleged partnership, T. H. Brodhead Company, as revised above:		
Territorial income taxes overstated		924.21
Gross income taxes overstated		217.22
Business income increased for the calendar year 1942		$ 40,624.38

(b) Contributions of $22.00 were reported on the partnership return of the alleged partnership, T. H. Brodhead Company, for the period 10-1-42 to 2-28-43, of which 92/151, or $13.40, are allocable to the calendar year 1942.

COMPUTATION OF TAX

Net income adjusted		$125,871.00
Less: Personal exemption	$ 1,200.00	
Credit for dependents	379.17	1,579.17
Balance (surtax net income)		$124,291.83
Less: Earned income credit—maximum		1,400.00
Balance subject to normal tax		$122,891.83
Normal tax at 6% on $122,891.83		$ 7,373.51
Surtax on $124,291.83		78,330.55
Income tax liability		$ 85,704.06

TAXABLE YEAR ENDED DECEMBER 31, 1943

ADJUSTMENTS TO NET INCOME

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return	$ 73,699.69	$ 74,888.57
Unallowable deductions and additional income		
(a) Business income increased	33,449.51	33,449.51
Total	$107,149.20	$108,338.08
Nontaxable income and additional deductions:		
(b) Contributions increased	585.64	none
Net income adjusted	$106,563.56	$108,338.08

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that the T. H. Brodhead Company, an alleged partnership between Thomas H. Brodhead and the Elizabeth S. Brodhead Trust, is not a valid partnership for Federal income tax purposes, and that all income from the T. H. Brodhead Company is taxable to you, with the result that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust is eliminated from such fiduciary return. In view of this determination, the income from the T. H. Brodhead Company,

which you reported on a fiscal year basis in line with the fiscal year basis used by the alleged partnership, must be adjusted to the calendar year basis used on your individual income tax returns. Accordingly, a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the period October 1, 1942 to February 28, 1943, and a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the fiscal year 3-1-43 to 2-29-44, is allocated to the calendar year 1943, based on the respective number of days in 1943. The computation of your revised business income from the alleged partnership, T. H. Brodhead Company, is as follows:

Ordinary net income reported on partnership return for the fiscal year 3-1-43 to 2-29-44		$ 96,790.88
Add: Legal fees drafting deed of trust erroneously charged to expense	$ 100.00	
Gross income taxes overstated	2,404.55	2,504.55
Ordinary net income for fiscal year 3-1-43 to 2-29-44 revised		$ 99,295.43
Pro-rata portion of $99,295.43 applicable to calendar year ending 12-31-44 (1-1-44 to 2-29-44): 60/366 of $99,295.43		16,277.94
Pro-rata portion of $99,295.43 applicable to calendar year ending 12-31-43 (3-1-43 to 12-31-43): 306/366 of $99,295.43		$ 83,017.49
Add: Pro-rata portion of $64,803.54, representing revised net income for period 10-1-42 to 2-28-43, applicable to calendar year ending 12-31-43 (1-1-43 to 2-28-43): 59/151 of $64,803.54		25,320.59
Revised business income from T. H. Brodhead Company for 1943		$108,338.08
Less: Business income reported on your 1943 return		74,888.57
Business income increased for the calendar year 1943		$ 33,449.51

(b) Contributions were reported on the partnership returns of the alleged partnership, T. H. Brodhead Company, in the amount of $22.00 for the period 10-1-42 to 2-28-43, and in the amount of $716.50 for the fiscal year 3-1-43 to 2-29-44, which are allocable to the calendar year 1943 on a prorated basis as follows:

59/155 of $22.00	$ 8.60	
306/366 of $716.50	599.04	
Total allowable	$ 607.64	
Reported from above sources on your return	22.00	
Contributions increased	$ 585.64	

COMPUTATION OF INCOME AND VICTORY TAX

Income tax net income adjusted		$106,563.56
Less: Personal exemption	$ 1,200.00	
Credit for dependents	700.00	1,900.00
Surtax net income		$104,663.56
Less: Earned income credit—maximum		1,400.00
Balance subject to normal tax		$103,263.56
Normal tax at 6% on $103,263.56		$ 6,195.81
Surtax on $104,663.56		62,824.21
Total income tax		$ 69,020.02
Victory tax net income adjusted	$108,338.08	
Less: Specific exemption	624.00	
Income subject to victory tax	$107,714.08	
Victory tax before credit (5% of $107,714.08)	$ 5,385.70	
Less: Victory tax credit—maximum	1,200.00	
Net victory tax		4,185.70
Net income and victory tax (1)		$ 73,205.72
Income tax for 1942 (2)		$ 85,704.06

Amount of item (1) or (2) whichever is larger		$ 85,704.06
Forgiveness feature:		
(a) Amount of item (1) or (2) whichever is smaller	$ 73,205.72	
(b) Amount forgiven — 75% of $73,205.72	54,904.29	
(c) Amount unforgiven		18,301.43
Correct income and victory tax liability		$104,005.49
Income and victory tax liability disclosed by return, Account No. 901221	$ 62,830.74	
Add: Deficiency assessed List Aug 3-513305-45	1,305.86	
	$ 64,136.60	
Less: Credit section 3806(b) I.R.C.—1945	2,412.00	61,724.60
Deficiency in income tax		$ 42,280.89

TAXABLE YEAR ENDED DECEMBER 31, 1944

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return	$ 54,550.25
Unallowable deductions and additional income:	
(a) Business income increased	95,106.88
Total	$149,657.13
Brought forward	$149,657.13
Nontaxable income and additional deductions:	
(b) Contributions increased	4,250.50
Net income adjusted	$145,406.63

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that the T. H. Brodhead Company, an alleged partnership between Thomas H. Brodhead and the Elizabeth S. Brodhead Trust, is not a valid partnership for Federal income tax

purposes, and that all income from the T. H. Brodhead Company is taxable to you, with the result that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust is eliminated from such fiduciary return. In view of this determination, the income from the T. H. Brodhead Company, which you reported on a fiscal year basis in line with the fiscal year basis used by the alleged partnership, must be adjusted to the calendar year basis used on your individual income tax returns. Accordingly, a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the fiscal year 3-1-43 to 2-29-44, and a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the fiscal year 3-1-44 to 2-28-45, is allocated to the calendar year 1944, based on the respective number of days in 1944. The computation of your revised business income from the alleged partnership, T. H. Brodhead Company, is as follows:

Ordinary net income reported on partnership return for the fiscal year 3-1-44 to 2-28-45	$153,829.06
Add: Gross income taxes overstated	6,871.59
Ordinary net income for fiscal year 3-1-44 to 2-28-45 revised	$160,700.65
Pro-rata portion of $160,700.65 applicable to calendar year ending 12-31-45 (1-1-45 to 2-28-45) : 59/365 of $160,700.65	25,976.27
Pro-rata portion of $160,700.65 applicable to calendar year ending 12-31-44 (3-1-44 to 12-31-44) : 306/365 of $160,700.65	$134,724.38
Add: Pro-rata portion of $99,295.43, representing revised net income for fiscal year 3-1-43 to 2-29-44, applicable to calendar year ending 12-31-44 (1-1-44 to 2-29-44) : 60/366 of $99,295.43	16,277.94
Revised business income from T. H. Brodhead Company for 1944	$151,002.32
Less: Business income reported on your 1944 return	55,895.44
Business income increased for the calendar year 1944	$ 95,106.88

(b) Contributions were reported on the partnership returns of the alleged partnership, T. H. Brodhead Company, in the amount of $716.50 for the fiscal year 3-1-43 to 2-29-44, and in the amount of $5,423.50 for the fiscal year 3-1-44 to 2-28-45, which are allocable to the calendar year 1944 on a prorated basis as follows:

60/366 of $716.50	$	117.46
306/365 of $5,423.50		4,546.82
Total allowable	$	4,664.28
Reported from above sources on your return		413.78
Contributions increased	$	4,250.50

COMPUTATION OF TAX

Net income adjusted	$145,406.63	
Less: Surtax exemptions	2,000.00	
Surtax net income	$143,406.63	
Surtax on $143,406.63		$105,951.90
Net income adjusted	$145,406.63	
Less: Normal tax exemption	500.00	
Balance subject to normal tax	$144,906.63	
Normal tax at 3% on $144,906.63		4,347.20
Correct income tax liability		$110,299.10
Income tax liability disclosed by return, Account No. 300431		30,354.20
Deficiency in income tax		$ 79,944.90

TAXABLE YEAR ENDED DECEMBER 31, 1945

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return	$ 81,134.23
Unallowable deductions and additional income:	
(a) Business income increased	55,690.75
Total	$136,824.98

Nontaxable income and additional deductions:		
(b) Contributions increased	$ 1,395.11	
(c) Net capital loss	501.75	1,896.86
Net income adjusted		$134,928.12

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that the T. H. Brodhead Company, an alleged partnership between Thomas H. Brodhead and the Elizabeth S. Brodhead Trust, is not a valid partnership for Federal income tax purposes, and that all income from the T. H. Brodhead Company is taxable to you, with the result that the income from the T. H. Brodhead Company reported on a fiduciary return filed for the Elizabeth S. Brodhead Trust is eliminated from such fiduciary return. In view of this determination, the income from the T. H. Brodhead Company, which you reported on a fiscal year basis in line with the fiscal year basis used by the alleged partnership, must be adjusted to the calendar year basis used on your individual income tax returns. Accordingly, a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the fiscal year 3-1-44 to 2-28-45, and a portion of the income reported by the alleged partnership, T. H. Brodhead Company, for the fiscal year 3-1-45 to 2-28-46, is allocated to the calendar year 1945, based on the respective number of days in 1945. The computation of your revised business income from the alleged partnership, T. H. Brodhead Company, is as follows:

Ordinary net income reported on partnership return for the fiscal year 3-1-45 to 2-28-46	$137,926.84
Less: Additional gross income taxes	3.35
Ordinary net income for fiscal year 3-1-45 to 2-28-46 revised	$137,923.49
Brought forward	$137,923.49
Pro-rata portion of $137,923.49 applicable to calendar year ending 12-31-46 (1-1-46 to 2-28-46) : 59/365 of $137,923.49	22,294.48
Pro-rata portion of $137,923.49 applicable to calendar year ending 12-31-45 (3-1-45 to 12-31-45) : 306/365 of $137,923.49	$115,629.01

Add Pro-rata portion of $160,700.65, representing revised net income for fiscal year 3-1-44 to 2-28-45, applicable to calendar year ending 12-31-45 (1-1-45 to 2-28-45) : 59/365 of $160,700.65.....	25,976.27
Revised business income from T. H. Brodhead Company for 1945	$141,605.28
Less: Business income reported on your 1945 return	85,914.53
Business income increased for the calendar year 1945	$ 55,690.75

(b) Contributions were reported on the partnership returns of the alleged partnership, T. H. Brodhead Company, in the amount of $5,423.50 for the fiscal year 3-1-44 to 2-28-45, and in the amount of $4,231.44 for the fiscal year 3-1-45 to 2-28-46, which are allocable to the calendar year 1945 on a prorated basis as follows:

59/365 of $5,423.50	$ 876.68
306/365 of $4,231.44	3,547.45
Total allowable	$ 4,424.13
Reported from above sources on your return	3,029.02
Contributions increased	$ 1,395.11

(c) Loss on sale of 50 shares Crandall-McKenzie & Henderson, Inc., previously unreported:

Cost 12-14-28	$1,300.00
Selling price 7-21-45....	296.50
Long-term capital loss..	$1,003.50
50% of $1,003.50 to be taken into account and allowable as a deduction	$ 501.75

COMPUTATION OF TAX

Net income adjusted	$134,928.12	
Less: Surtax exemptions	2,500.00	
Surtax net income	$132,428.12	
Surtax on $132,428.12		$ 96,181.03
Net income adjusted	$134,928.12	
Less: Normal tax exemptions	1,000.00	
Balance subject to normal tax	$133,928.12	
Normal tax at 3% on $133,928.12		4,017.84
Correct income tax liability		$100,198.87
Income tax liability disclosed by return, Account No. 300312		51,532.76
Deficiency in income tax		$ 48,666.11

[Endorsed]: T.C.U.S. Filed July 3, 1950.

[Title of Tax Court and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioners admits and denies as follows:

I, II and III. Admits the allegations contained in paragraphs I, II and III of the petition.

IV and IV-1 to 20, inclusive. Denies that the Commissioner erred in the determination of the deficiencies as alleged in paragraph IV of the petition and subparagraphs 1 to 20, inclusive, thereunder.

V-1. Denies the allegations contained in subpara-

graph 1 of the petition except it is admitted that an extension of time for the assessment of said tax was executed extending the time for assessment to June 30, 1950.

2 to 19, inclusive. Denies the allegations contained in subparagraphs 2 to 19, inclusive, of paragraph V of the petition.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioners' appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:
B. H. NEBLETT, Division Counsel;
T. M. MATHER, Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Aug. 8, 1950.

[Title of Tax Court and Cause.]

AMENDMENT TO ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and, pursuant to leave first had and obtained, amends the answer in the above-entitled proceeding by inserting immediately following paragraph V of the answer the following paragraph:

VI. Further answering, respondent alleges:

1. That on or about March 20, 1944, the petitioners filed with the Collector of Internal Revenue

for the collection district of Hawaii a Federal income tax return, Form 1040, for the calendar year 1943;

2. That the gross income stated on said return was in the amount of $74,888.57;

3. That petitioners omitted from gross income on said return an amount properly includable therein which is in excess of twenty-five per centum of the amount of gross income stated in said return, and by reason thereof the provisions of Section 275(c) of the Internal Revenue Code are applicable to the tax for said year.

4. That on or about January 18, 1949, the petitioners and the Commissioner of Internal Revenue executed a consent extending to June 30, 1950, the period within which an income tax may be assessed or a deficiency notice mailed to the petitioners for the calendar year 1943.

/s/ CHARLES OLIPHANT,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
C. W. NYQUIST,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: T. C. U. S. Filed June 20, 1951.

The Tax Court of the United States

Docket No. 29391

THOMAS H. BRODHEAD and
ELIZABETH S. BRODHEAD,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 29392

THOMAS H. BROADHEAD and
ELIZABETH S. BRODHEAD,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STIPULATION OF FACTS

It is hereby stipulated and agreed, by and between the parties hereto, by their respective attorneys, that the following facts shall be taken as true and may be received by the Court in evidence with the same force and effect as if the facts herein contained were testified to by competent witnesses; provided, however, that this stipulation shall be without prejudice to the right of either party to introduce other or further evidence not inconsistent with the facts herein stipulated as true:

I.

That petitioners Thomas H. Brodhead and Elizabeth S. Brodhead are, and were at all times material to this proceeding, husband and wife and residents of the Territory of Hawaii.

II.

That petitioners have three children, Virginia Holmes Brodhead, born December 29, 1939, Barbara Jane Brodhead, born November 19, 1942, and Thomasene Elizabeth Brodhead, born May 1, 1945.

III.

That petitioner Thomas H. Brodhead, on September 30, 1942, created the Thomas H. Brodhead Trust, naming Mortimer J. Glueck and Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, as Trustees. A true copy of Trust Indenture, dated the 30th day of September, 1942, marked Exhibit 1, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

IV.

That a document entitled a Special Partnership Agreement, dated as of the 30th day of September, 1942, was duly executed by Thomas Holmes Brodhead, described as General Partner therein, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, described as Special Partner therein. A true copy of said Special Partnership Agreement,

marked Exhibit 2, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

V.

That a Bill of Sale, dated as of the close of business on September 30, 1942, was duly executed by Thomas Holmes Brodhead, as Seller, and T. H. Brodhead Company, a Special Partnership, as Buyer. A true copy of said Bill of Sale, marked Exhibit 3, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VI.

That on December 23, 1942, a duly executed Certificate of Special Partnership and Affidavits of Thomas Holmes Brodhead, Mortimer J. Glueck, and W. A. White, required by Section 6875, Revised Laws of Hawaii 1935, were duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935. A true copy of said Certificate and Affidavits, marked Exhibit 4, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VII.

That a Statement of Substance of Certificate of Special Partnership was duly published in The Honolulu Advertiser on December 30 and 31, 1942, and January 6 and 7, 1943.

VIII.

The Elizabeth S. Brodhead Trust, with said Mor-

timer J. Glueck and Bishop Trust Company, Limited, named as Trustees, was created on February 28, 1943. A true copy of Trust Indenture dated the 28th day of February, 1943, marked Exhibit 5, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

IX.

That on February 28, 1943, the Elizabeth S. Brodhead Trust purchased from the Thomas H. Brodhead Trust all of its right, title and interest in and to its 50% capital interest in the Special Partnership known as "T. H. Brodhead Co.", which was duly assigned to said Elizabeth S. Brodhead Trust by Assignment dated the 28th day of February, 1943. A true copy of said Assignment, marked Exhibit 6, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

X.

That the Elizabeth S. Brodhead Trust gave to the Thomas H. Brodhead Trust its note for the unpaid balance of the purchase price of its interest in T. H. Brodhead Co. in the amount of $30,000.00 with interest at 5% per annum. Interest was paid periodically, and said note was paid off by payments of $5,000.00 on June 9, 1945, of $5,000.00 on November 26, 1945, of $17,500.00 on June 22, 1949, and the balance of $2,500.00 on September 9, 1949.

XI.

That on May 5, 1943, a duly executed Certificate of Change of Special Partnership and Affidavits of

Thomas Holmes Brodhead, Mortimer J. Glueck, and W. A. White, required by Section 6875, Revised Laws of Hawaii 1935, were duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935. A true copy of said Certificate and Affidavits, marked Exhibit 7, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XII.

That a Statement of the Substance of Certificate of Change of Special Partnership was duly published in The Honolulu Advertiser on May 12, 13, 19 and 20, 1943.

XIII.

That a document entitled Amendment of Special Partnership Agreement, changing the name of said special partnership from "T. H. Brodhead Co." to "Ace Distributors", dated as of the close of business of the 28th day of February, 1947, was duly executed by Thomas Holmes Brodhead, described as General Partner therein, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead, as Settlor, described as Special Partner therein. A true copy of said Amendment, marked Exhibit 8, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIV.

That on February 28, 1947, a Certificate of Change of Special Partnership was duly filed in the Office

of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935. A true copy of said Certificate, marked Exhibit 9, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XV.

That a Statement of the Substance of Certificate of Change of Special Partnership was duly published in The Honolulu Advertiser on March 7, 8, 14 and 15, 1947.

XVI.

That as of the close of business on February 28, 1947, Ace Distributors (formerly T. H. Brodhead Co.) duly assigned to T. H. Brodhead Co., Ltd., a Hawaiian corporation, certain rights, property, assets and privileges, subject to certain liabilities, obligations, and indebtedness, having a net book value of $80,000.00, in full payment of 4,000 shares of stock of said corporation to be issued to each of Thomas Holmes Brodhead and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead, as Settlor; that on February 28, 1947, there was filed in the Office of the Treasurer of the Territory of Hawaii, in the matter of the incorporation of T. H. Brodhead Co., Ltd., an Affidavit of Officers, setting forth the subscribers to the capital stock of the corporation and the manner in which payment for the stock had been made, to which is attached the Bill of Sale

of Ace Distributors to T. H. Brodhead Co., Ltd., referred to above. A true copy of said Affidavit of Officers and Bill of Sale attached, marked Exhibit 10, is attached hereto, incorporated herein by reference, and made part hereof for all purposes.

XVII.

That T. H. Brodhead Co. filed its partnership tax returns on an accrual and fiscal year basis ending on the 28th day of February, and filed its first return on that basis for the fiscal year ended February 28, 1943. Photostatic copies of the partnership returns for the fiscal years ended February 28, 1943, February 28, 1944, February 28, 1945, February 28, 1946, February 28, 1947, February 28, 1948, and February 28, 1949, marked Exhibits 11, 12, 13, 14, 15, 16 and 17, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XVIII.

That Schedules showing the income and expenses for the period from September, 1942, to September 30, 1950, and the inventory of assets of the Thomas H. Brodhead Trust at September 30, 1950, as shown by the books and records of said Trust, marked Exhibits 18 and 19, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIX.

That Schedules showing the income and expenses for the period from February 28, 1943, to February 28, 1951, the payments received as distributions of

its share of income of T. H. Brodhead Co. and/or Ace Distributors, and the inventory of assets of the Elizabeth S. Brodhead Trust at February 28, 1951, as shown by the books and records of said Trust, marked Exhibits 20, 21 and 22, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XX.

That the Thomas H. Brodhead Trust and Elizabeth S. Brodhead Trust filed federal fiduciary returns each year and duly paid the tax shown to be due thereon. Schedules showing the items of income and deductions shown on said tax returns of Thomas H. Brodhead Trust and Elizabeth S. Brodhead Trust, marked Exhibits 23 and 24, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes. Photostatic copies of the fiduciary tax returns filed by said Thomas H. Brodhead Trust for the years 1943, 1944, 1945, 1946, 1947, 1948 and 1949, marked Exhibits 25, 26, 27, 28, 29, 30 and 31, respectively, and by said Elizabeth S. Brodhead Trust for the same years, marked Exhibits 32, 33, 34, 35, 36, 37 and 38, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXI.

That photostatic copies of the joint tax returns filed by petitioners for the years 1942, 1943, 1944, 1945 and 1948, of petitioner Thomas H. Brodhead for the year 1946, and of petitioner Elizabeth S.

Brodhead for the year 1946, marked Exhibits 39, 40, 41, 42, 43, 44 and 45, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

/s/ MILTON CADES,
Counsel for Petitioners,

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

EXHIBIT No. 1

(Deed of Trust dated September 30, 1942
Thomas Holmes Brodhead)

This indenture, made this 30th day of September, 1942, by and between Thomas Holmes Brodhead, who is a citizen of the United States of America, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter called the "Settlor," and Mortimer J. Glueck, of Honolulu aforesaid, who is a citizen of the United States of America, and Bishop Trust Company, Limited, a corporation duly organized and existing under the laws of the Territory of Hawaii and a majority of whose officers and directors are citizens of the United States of America, hereinafter called the "Trustees,"

Witnesseth that:

The Settlor, in consideration of the love and affection he bears the beneficiaries and of the acceptance by the Trustees of the trust herein created,

Exhibit No. 1—(Continued)

does hereby transfer, set over and deliver to the Trustees, their successors in trust and assigns, the sum of Forty Thousand and No/100ths Dollars ($40,000.00);

To have and to hold the same, together with all other property which may hereafter be or become a part of the trust estate hereby created, unto the Trustees, their successors in trust and assigns, in trust nevertheless for the uses and purposes hereinafter stated, that is to say:

(a) The Trustees shall contribute the sum of Forty Thousand and No/100ths Dollars ($40,000.00) to the capital of the partnership known as "T. H. Brodhead Co.," a special partnership to be duly organized concurrently herewith under that certain Special Partnership Agreement dated September 30, 1942, for a fifty per cent (50%) interest therein, and continue to be a special partner in such partnership, said sum being the fair and reasonable value of said interest duly ascertained as of September 30, 1942;

(b) The Trustees shall accumulate all net income from the said trust estate during the continuation of this trust; provided, however, that the Trustees during such time may in their sole discretion pay out of the net income of said trust estate to or apply for the use and benefit of any of the children of the Settlor or the lawful issue of any of them who shall die during the continuance of this trust, such amounts as may be necessary for their maintenance, support and education; and all in-

Exhibit No. 1—(Continued)

come not so distributed in any calendar year shall at the end of such year be added to and become a part of the corpus of the trust estate;

(c) The Trustees are hereby authorized and empowered to pay from the corpus of the said trust estate any sum or sums from time to time and for such periods of time as in their sole discretion they shall deem necessary or proper for the support, maintenance and education of any of the children of the Settlor whenever the Trustees in their sole discretion deem the income which any of them are receiving insufficient for such purposes; and such payment shall not be deemed an advancement of corpus to any child and the Trustees shall be under no obligation in such use of corpus to pay or use corpus equally or proportionately for said child and all payments from the corpus of the trust estate shall be binding upon all beneficiaries hereunder;

(d) The Trustees are hereby authorized and empowered to pay to any child of the Settlor at any time after said child shall attain the age of twenty-one (21) years, as the Trustees in their sole discretion shall deem proper, such portion of the corpus of the trust estate and the accumulated income thereof as shall constitute one share thereof, such share to be determined by considering the trust estate as being divided into as many equal shares as there shall be children of the Settlor then surviving or lineal descendants of any deceased child, one share for each living child and one share for the lineal descendants of each deceased child;

Exhibit No. 1—(Continued)

(e) This trust shall cease and determine twenty (20) years after the date of the death of the Settlor, and the Trustees shall thereupon transfer, set over and deliver all the property then comprising the trust estate and all accumulated income thereof to the children of the Settlor (other than those to whom distribution of a share of the trust estate may have been made in accordance with the provisions of subparagraph (d) hereinabove), and the lawful issue of any of the children of the Settlor who shall have died prior to the termination of the said trust estate, in equal shares, per stirpes and not per capita, absolutely and free and clear of any trust, and in the event that upon the death of the last survivor of the children of the Settlor there be no lawful issue of said children then surviving, then the said property and income shall at such time vest in and be transferred, conveyed and delivered by the Trustees, absolutely and in fee simple to those persons other than the Settlor who would be the heirs at law of the last survivor of the children of the Settlor under the statutes of descent of the Territory of Hawaii in full force and effect at the time of his or her death, the same as if he or she had died intestate at that time; provided, however, that in the event the partnership known as "T. H. Brodhead Co." shall terminate during the continuance of this trust, the Trustees may determine this trust at any time thereafter which to the Trustees may seem best, and thereupon the property comprising the said trust estate, together with

Exhibit No. 1—(Continued)

the accumulated income thereof, shall vest in and be transferred, conveyed and delivered by the Trustees absolutely and in fee simple, free and clear from any trusts in equal shares to those who are surviving of the children of the Settlor (other than those to whom distribution of a share of this trust estate may have been made in accordance with the provisions of subparagraph (d) hereinabove), and the lawful issue of any of said children who shall then be dead, said issue to take per stirpes and not per capita;

(f) The Trustees shall receive, hold, manage and control the said trust estate, collect the income therefrom and pay all charges incident to trust estates and properly payable by said trust estate therefrom; and the Settlor authorizes the Trustees to retain either permanently or temporarily or for such period of time as they may deem expedient any property conveyed, assigned or delivered to the Trustees by the Settlor of whatever nature; and the Settlor directs that the said Trustees shall not be held liable for any loss resulting to said trust estate by reason of the Trustees' retaining any such property or for any error of judgment in this respect;

(g) The Settlor authorizes and empowers the Trustees to sell at public or private sale, convert, transfer, exchange, mortgage, hypothecate and otherwise deal in or dispose of the whole or any part of the property, real, personal and mixed, which may be from time to time a part of the trust

Exhibit No. 1—(Continued)

estate, with power to accept any purchase money mortgage or mortgages for any part of the purchase or exchange price; to invest and reinvest the whole or any part of the assets of the said trust estate, and in investing and reinvesting any assets of said trust estate the Trustees may invest in common or preferred stocks of corporations, bonds, notes, debentures, participation or investment certificates and/or in any other property, real or personal, in so far as in their judgment they shall deem such investments advisable, it being the intention of the Settlor, under the foregoing provisions, to grant to the Trustees full power to invest and reinvest money in such investments as they shall deem desirable and suitable investments for trust funds without being restricted to the classes of investments which trustees are permitted by law to make, provided, however, that the Trustees shall obtain the consent of the Settlor to make such investments during his lifetime, and provided further that in the event the Settlor shall die before the termination hereof, the Trustees shall thereafter be restricted in the making of investments of trust funds to the classes of investments which trustees are permitted by law to make, except that in any event the Trustees may, without liability for any losses resulting therefrom, make advances or loans to the partnership known as "T. H. Brodhead Co." the Settlor authorizes and empowers the Trustees, upon any increase of the capital stock of any corporation in which said trust estate shall own shares,

Exhibit No. 1—(Continued)

to exercise any preemptive rights to such shares to which said trust estate may be liable and/or to subscribe for such additional shares as in the judgment of the Trustees shall be an advisable investment; and for this purpose and for other purposes of this trust, the Settlor authorizes and empowers the Trustees to borrow money either from themselves or from others and upon such terms and conditions as they may deem appropriate; the Trustees shall have the right and power to vote either directly or by proxy the stock of any corporation that may be a part of said trust estate from time to time at all meetings of stockholders as the Trustees may deem best;

(h) Stock dividends shall be treated as capital of the trust estate and all stock acquired by the Trustees under the exercise of rights to subscribe or the net proceeds realized by the Trustees from the sale of rights to subscribe shall be treated as capital of the trust estate and all other corporate distribution shall be treated as income; provided, however, that where a distribution is made through the reduction of any corporate stock held by the Trustees, or, in the exclusive discretion of the Trustees it appears to be made in or as a result of a partial or complete liquidation or dissolution of the corporation, the Trustees may in their discretion make such apportionment of any such distribution between income and capital as to them may seem just; the Trustees shall have full power and authority to decide and determine in all doubtful

Exhibit No. 1—(Continued)

cases what property or moneys received by them is capital and what is income; and also in all doubtful cases to decide and determine what expenses and other charges are payable out of income and what out of capital; and also in all doubtful cases to decide and determine what proportion of payments for expenses of or charges against the trust estate are payable from income and what from capital; and all beneficiaries shall be bound by the decision and determination of the Trustees in regard to all such allocations between capital and income; the Trustees shall have authority in and discretion to prorate during the year and withhold from the income received by the trust estate an amount sufficient to pay proportionate shares of the expenses payable by the trust estate so that said payments of net income may be more regular and even in amount, and to withhold such amounts of income and/or principal as they may deem necessary to protect themselves from any possible liability for taxes and/or costs or expenses in connection with or arising out of possible claims therefor;

(i) The Settlor may transfer, convey and assign to the Trustees any property in addition to that hereinbefore referred to, to be held upon the trust hereby created, and thereafter such additional property shall be and form a part of the trust estate;

(j) The Trustees shall render annual statements of account to the persons who are the beneficiaries of this trust, as hereinabove provided, but the Trustees shall not be required to account in any court

Exhibit No. 1—(Continued)

unless requested so to do by a beneficiary; provided, however, that the Trustees may whenever they shall deem it advisible file accounts in any court having jurisdiction thereof for approval, the costs of said proceeding to be paid out of the trust estate;

(k) If any person entitled to receive any of the income and/or capital of the trust estate shall be a minor, the Trustees may pay the share of income and/or capital to which said minor is entitled to either parent of or to the natural or legally appointed guardian of such minor, and the receipt of such parent or natural or legally appointed guardian shall be a complete release, discharge and acquittance of the Trustees to account further for any payment or payments so made, and if any beneficiary is a minor, the statements of account may be furnished to either parent of or to the natural or legally appointed guardian of such minor beneficiary;

(l) Bishop Trust Company, Limited, the corporate Trustee, hereunder, shall have the custody and safekeeping of all moneys and securities belonging to the trust estate which are received or collected by the Trustees. Neither Trustee hereunder shall be answerable or accountable for any act of the other Trustee in which he or it shall not participate, nor for the custody of any property except as shall come to his or its own possession or personal control, nor for any loss or damage resulting from any error of judgment or otherwise except through his or its own gross neglect or wilful

Exhibit No. 1—(Continued)

default. Nor shall the Trustees or either of them be answerable or accountable for any loss or damage resulting from any act consented to by the Settlor or for any loss or damage resulting from any investment in or loan or advance to the partnership of "T. H. Brodhead Co";

(m) No beneficiary hereunder shall have the power or authority to anticipate in anywise any of the rents, issues, profits, income, moneys or payments herein provided to be devoted or paid to him or her or any part thereof, nor to alienate, encumber, convey, transfer or dispose of the same or of any interest therein or part thereof, in advance of payment; nor shall the same be involuntarily alienated by him or her or be subject to attachment or execution or be levied upon or taken upon any process for any debts which any such beneficiary shall have contracted or in satisfaction of any demands or obligations which he or she shall incur. All payments or distribution of either income and/or principal as hereinabove provided shall be made by the Trustees and subject to the provisions of subparagraph (k) hereinabove shall be valid and effectual only when made to the beneficiary to whom the same shall appertain and belong, and upon his or her individual receipt; provided, however, that when and while the person so entitled to receive such payment shall be without the bounds of the Territory of Hawaii, such payment may be made to any formally appointed agent of such person, but only upon the personal receipt above provided for;

Exhibit No. 1—(Continued)

(n) In the event that Mortimer J. Glueck shall be or become unable to act or shall decline to act or shall resign his office as Co-trustee hereunder, or from and after the death of Mortimer J. Glueck prior to the termination of this trust, then and in any of such events, Edouard R. L. Doty shall be substituted as Co-trustee in his place and stead and in the event that Edouard R. L. Doty shall be or become unable to act or shall decline to act or shall resign his office as Co-trustee hereunder or from and after the death of Edouard R. L. Doty prior to the termination of the trust, Bishop Trust Company, Limited, may select some person to be substituted as Trustee in the place and stead of Edouard R. L. Doty, and title to all property then comprising the trust estate shall be vested in such person and Bishop Trust Company, Limited, as Trustees without any conveyance or vesting order;

(o) It is hereby declared that this agreement shall be and is hereby made irrevocable by the Settlor and the Settlor reserves the right to amend this instrument only by adding other property to be and become a part of the estate held under the terms hereof, and the right to alter, amend, cancel or revoke any provisions of this instrument, save and except paragraphs (a), (b), (c), (d), and (e), hereof; provided, however, that in no event shall any of the property or the income thereof belonging to the trust estate be paid to or inure to the benefit of the Settlor, and provided further that any amendments made by the Settlor shall be made

Exhibit No. 1—(Continued)

by instrument in writing and acknowledged and filed with the Trustees, and that the alteration, amendment, cancellation or revocation of any provision of this instrument shall be made only with the written consent and approval of the Trustees and of all the beneficiaries hereunder;

The said Mortimer J. Glueck and Bishop Trust Company, Limited, hereby accept the within trust and covenants and agree with the Settlor that they will faithfully discharge and carry out the same.

In witness whereof, the parties hereto have executed these presents the day and year first above written.

/s/ THOMAS HOLMES BRODHEAD,
Settlor.

/s/ MORTIMER J. GLUECK, and
BISHOP TRUST COMPANY,
LIMITED,

/s/ By W. A. WHITE,
Its Vice President.

[Seal] /s/ By E. BENNER, JR.,
Its Asst. Vice Pres.,
Trustees.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who

Exhibit No. 1—(Continued)

executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Mortimer J. Glueck, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Assistant Vice President respectively of Bishop Trust Company, Limited, a Hawaiian corporation, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Di-

Exhibit No. 1—(Continued)

rectors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

EXHIBIT No. 2

This special partnership agreement, dated as of the 30th day of September, 1942, made by and between Thomas Holmes Brodhead, of Honolulu, City and County of Honolulu, Territory of Hawaii, a citizen of the United States of America, hereinafter referred to as "General Partner," and Mortimer J. Glueck, of Honolulu aforesaid, a citizen of the United States of America, and Bishop Trust Company, Limited (a corporation organized and existing under the laws of the Territory of Hawaii and a majority of whose officers and directors are citizens of the United States of America), Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, as Settlor, hereinafter referred to as "Special Partner,"

Witnesseth That:

The parties hereto, having mutual confidence in each other, do hereby form with each other a Special Partnership for the purpose of acquiring and thereafter conducting the business heretofore carried on by Thomas Holmes Brodhead and known as "T. H. Brodhead," from and after the close of business on September 30, 1942, and for other pur-

Exhibit No. 2—(Continued)

poses as hereinafter provided upon the following terms and conditions, that is to say:

1. Purposes: The purposes of the partnership shall be to acquire as at the close of business on September 30, 1942, all the assets and to carry on the business heretofore carried on and conducted by Thomas Holmes Brodhead under the name of "T. H. Brodhead;" to buy, sell, import, trade and deal in goods, wares and merchandise of every kind and nature and to engage in and carry on the business of wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers; to buy or otherwise acquire, own, hold, use, improve, develop, mortgage, lease or take on lease, sell, convey and in any and every other manner deal in and with and dispose of real estate, buildings and other improvements, hereditaments, easements and appurtenances of every kind in connection therewith, or any estate or interest therein of any tenure or description to the fullest extent permitted by law, and also any and all kinds of chattels, goods, wares, merchandise and agricultural, manufacturing and mercantile products and commodities and patents, licenses, debentures, securities, stocks, bonds, commercial paper, and other forms of assets, rights, and interests and evidences of property or indebtedness, tangible or intangible; to undertake and carry on any business investment, transaction, venture or enterprise which may lawfully be undertaken or carried on by a partnership and any business whatsoever which may seem to the partnership convenient or suitable to

Exhibit No. 2—(Continued)

be undertaken whereby, directly or indirectly, to promote any of its general purposes or interests or render more valuable or profitable any of its property, rights, interests or enterprises; and to acquire by purchase, lease or otherwise the property, rights, franchises, assets, business and good will of any person, firm, corporation or association engaged in or authorized to conduct any business or undertaking which may be carried on by this partnership or possessed of any property suitable or useful for any of its own purposes and carry on the same, and undertake all or any part of the obligations and liabilities in connection therewith on such terms and conditions and for such consideration as may be agreed upon and to pay for the same either all or partly in cash, stocks, bonds, debentures or other forms of assets or securities; and to effect any such acquisitions or carry on any business authorized by this agreement either by directly engaging therein or indirectly by acquiring the shares, stocks or other securities of such other business or entity and holding and voting the same and otherwise exercising and enjoying the rights and advantages incident thereto and such other business as may be necessary, suitable or proper to the accomplishment of their purposes or connected or related thereto, as the partners from time to time mutually may agree.

2. Name: The partnership shall be conducted and carried on under the firm name and style of "T. H. Brodhead Co.," and the place or places of business

Exhibit No. 2—(Continued)

shall be at Honolulu aforesaid, and/or at such other place or places as the partners may from time to time determine.

3. Capital: The capital of the partnership as of the date of the commencement of the term provided for in this agreement shall be the sum of $80,000.00, which amount represents the book value of the net assets acquired by the partnership as of September 30, 1942; and it is agreed that the contributions of capital of each of the partners to this agreement shall be as follows:

	Amount	Interest & Percentage
Thomas Holmes Brodhead	$40,000.00	50%
Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Thomas Holmes Brodhead dated September 30, 1942	$40,000.00	50%

It is understood and agreed that Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees as aforesaid, shall be a special partner in their capacity as Trustees and not individually, and shall have all powers, rights and duties of a special partner as prescribed by Chapter 225, Revised Laws of Hawaii 1935, as the same now is or as the same may from time to time be amended, and that the special partner shall not be liable for the debts of the partnership to any extent beyond that set forth in the provisions of Section 6887 of the Revised Laws of Hawaii 1935 as the same now is or as the same may from time to time be amended.

4. Compensation of general partner and division

Exhibit No. 2—(Continued)

of profits: From time to time and as the partners may agree, the general partner actively engaged in the business of the partnership shall receive as compensation for services rendered to the partnership a salary, chargeable for purposes of computing net profits hereunder, as an expense of the business, in such amount as the partners from time to time shall agree upon constituting the reasonable value of the services rendered to the partnership. All of the remaining net profits in the partnership shall be divided for each annual period in proportion to the above stated interest of each of the partners in the original capital of the partnership, and all losses of the partnership for each annual period shall be divided among the partners in the same manner as herein provided for the division of profits. Any partner may withdraw from the partnership such portion of the profits attributable to said partner's interest as the partners may from time to time deem advisable. Amounts not withdrawn shall not be added to the capital account but shall be credited to advance accounts in the names of the respective partners for whom said amounts are being held, and no interest shall be paid on said accounts.

5. Services of the partners: The general partner shall diligently give so much of his time, attention and services to the business of the partnership as shall be required, and shall be faithful to the partnership in all transactions relating to said business, and shall not employ the capital or credit of the partnership in any other business than that of the

Exhibit No. 2—(Continued)

partnership and shall not, during the continuation of the partnership, carry on or be concerned or interested directly or indirectly in any other business which is in direct competition with the business of the partnership.

6. Bankers of the partnership: The bankers of the partnership shall be Bank of Hawaii and/or such other bankers as the partners shall from time to time determine, and all money and money instruments received by and belonging to the partnership shall be deposited to the credit of the partnership account with the partnership bankers except that such a petty cash fund as may be mutually agreed upon between the partners from time to time may be kept on hand for use in the business.

7. Limitation on powers of partners: The general partner only shall have authority to transact the business of the partnership or incur obligations or liabilities and shall establish the policy of the partnership. The special partner at all times may investigate the partnership affairs and advise the general partner as to its management. The general partner shall not, without the consent of the other partner, draw, accept or sign any bill of exchange or promissory note or contract any debt on the part of the partnership or employ any of the money or effects thereof or in any manner pledge the credit thereof except in the usual course of the business subject to the provisions of this agreement; nor without obtaining the consent thereto of the other partner assume any liability for another or

Exhibit No. 2—(Continued)

others by means of endorsement or by becoming guarantor, surety or insurer.

8. Partners not to assign interest: The general partner shall not assign or mortgage his share of or interest in or any part of the shares of or interest in the partnership or the assets or profits thereof. The special partner may assign its share of or interest in the partnership only with the consent of the general partner evidenced by written consent attached to such assignment and filed in the office of the partnership, and the general partner shall have full power and discretion to give or withhold such consent.

9. Books of account and access thereto: Proper partnership books of account shall be kept by the general partner and entry shall be made therein of all transactions and all such matters and things as usually are entered in books of account kept by persons engaged in the same or similar businesses, such books of account and all documents, letters, papers, instruments and records belonging to the partnership shall be kept at the office of the partnership and each partner shall, at all times, have full and free access to examine and copy the same. The books of the partnership shall be audited periodically at such times as the partners shall determine but not less than once a year and copies of the Auditor's report shall be delivered to each partner.

10. Annual account: A general account shall be taken annually of the assets and liabilities of the partnership of all dealings and transactions of the

Exhibit No. 2—(Continued)

same during the preceding year of all matters and things usually included in accounts of a like nature taken by persons engaged in like businesses, and in taking such account a just valuation shall be made of all items requiring valuation, and such annual account shall state the capital of the partnership and the interest of each partner therein at the end of the period of the accounting, such general account to be sent to each partner, and unless within three (3) months any partner shall object to the same, the same shall be binding upon the partners except for manifest errors of fraud.

11. Determination of partnership: The partnership may be determined by the general partner at any time upon giving not less than two (2) months previous notice in writing to the other partner of his intention, and at the expiration of such notice, the partnership shall determine accordingly. Upon the determination of the partnership from whatever cause, the general partner agrees that he will make a true, just and final account of all things relating to said business and in all things duly adjust the same. After the affairs of the partnership are adjusted, its debts paid and discharged and the expense of liquidation shall have been paid, the balance then remaining shall be applied, first, in payment to such partner or his representative of the balance due to each partner as shown in the advance account of said partner, then in payment of his share of the capital as shown on the books of the partnership as of the close of business of the partnership, and the balance shall be divided in

Exhibit No. 2—(Continued)

the same manner as hereinabove provided for the division of profits. In the event that the balance remaining after the payment of said debts and expenses and the balance due to each partner as shown in the advance account of said partner is insufficient to pay the full capital account of all the partners, then such balance shall be applied, first, in payment to the special partner of its share of the capital as shown on the books of the partnership as at the close of business of the partnership, then in payment on account of the capital account of the general partner. In the event that the balance remaining after the payment of said debts and expenses is insufficient to pay in full the balance due to all the partners as shown in the advance account of each partner, then the amount shown as due to the special partner shall be paid first, and the remaining balance, if any, paid to the general partner on account of the balance shown in his advance account. The partners shall execute such instruments for facilitating and effecting the realization and the division of the assets of the partnership and for their mutual indemnity and release and otherwise as may be requisite or proper.

12. Death of General Partner: If the general partner shall die before the expiration of the partnership, his representative shall have the option (such option to be declared by notice in writing given to the special partner within six (6) months after his death) of succeeding to or carrying on the interest of the deceased partner in said business as a general partner in accordance with the

Exhibit No. 2—(Continued)

laws of the Territory of Hawaii, as the same now is or as the same may from time to time be amended; and if such option shall be exercised, the said business shall be carried on during the residue of said term as from the death of said general partner as nearly as may be according to the provisions of these presents, but so that the representative of said general partner shall succeed to his share in said business and be substituted for him as a general partner; provided that in case the representative of said general partner shall elect to become a general partner by virtue of such option, as aforesaid, all proper instruments for carrying out the provisions of this present clause shall be executed and made between the representative and the surviving partner, and all proper notices, publications, petitions of court proceedings shall be made, executed or taken at the expense of the partnership.

13. Winding up on death of general partner: In case the representative of said general partner shall not exercise his option to succeed to the deceased partner's share in said business as a general partner, then the partnership shall be wound up at the expiration of six (6) calendar months from the date of such death or such sooner time as the surviving partner and the representative of the deceased partner may agree upon and its affairs settled in the manner provided in paragraph 11 hereof.

14. Bankruptcy: If the general partner shall at any time during the partnership become incapacitated, bankrupt or insolvent or enter into any com-

Exhibit No. 2—(Continued)

position or arrangement with or for the benefit of his creditors, or commit any breach of any of the stipulations or agreements herein contained, the special partner may determine the partnership by giving notice in writing to such general partner and may publish notice of dissolution of the partnership without prejudice to its remedies for any incidental breach of any of the stipulations or agreements aforesaid.

15. Arbitration: If at any time during the continuance of the partnership or after the dissolution or termination thereof any dispute, difference or question shall arise between the partners touching the partnership or accounts or transactions thereof or the dissolution or winding up thereof or the construction, meaning or effect of these presents or anything herein contained, or the rights or liabilities of the partners under these presents or otherwise in relation to the premises, then every such dispute, difference or question shall, at the desire of either partner be submitted to and be determined by three arbitrators in the manner determined by Chapter 225, Revised Laws of Hawaii 1935, as the same now is or may from time to time be amended, in which case any partner may give to the other partner written notice of his or its desire to have an arbitration of the matter in dispute and name one of the arbitrators in said written notice, whereupon the other partner, within ten (10) days after the receipt of such notice, shall name a second arbitrator, and in case of failure to do so the arbitrator already appointed shall name such second arbitrator and the two arbitrators so ap-

Exhibit No. 2—(Continued)

pointed (in either manner) shall elect and appoint a third arbitrator, and in the event that any two arbitrators so appointed shall fail to appoint a third arbitrator within ten (10) days after the naming of the second arbitrator either party may have the third arbitrator selected or appointed by the person being the Chief Justice of the Supreme Court of the Territory of Hawaii, holding office at that time, and the three arbitrators so appointed shall thereupon proceed to determine the matter in question, disagreement or difference, and the decision of any two of them (including the disposition of the costs of arbitration) shall be final, conclusive and binding upon all parties unless the same shall be vacated or corrected as by said statute provided. The arbitrators shall have the powers and duties prescribed by said statute and judgment may be entered upon any such award by the Circuit Court of the First Judicial Circuit as provided in said statute.

16. Amendments: If at any time during the continuance of this partnership the parties hereto shall deem it necessary or expedient to make any amendment in any article, clause, matter or thing herein contained for the more advantageous or satisfactory management of the partnership business, it shall be lawful for them so to do by any writing under their joint hands, endorsed on these articles or entered in any of the partnership books and all such alterations shall be adhered to and have the same effect from and after the adoption of the same as if the same had originally been embodied in and formed a part of these presents.

17. Term of partnership: The term of the part-

Exhibit No. 2—(Continued)

nership shall be for a period commencing as of October 1, 1942, and ending September 30, 1952, and subject to the provisions of paragraphs 11 and 13 hereinabove, shall continue from year to year ending on the 30th day of September of each year thereafter until terminated by either partner giving not less than three (3) months' written notice of his or its intention to terminate the partnership to the other partner.

18. Definitions: The term "General Partner" as used herein shall include the heirs, executors, administrators and assigns of the general partner, and the term "Special Partner" as used herein shall include said Mortimer J. Glueck and Bishop Trust Company, Limited, in their capacity as Trustees under Deed of Trust dated September 30, 1942, and not in their individual capacity, and their successors in trust and assigns, and the term "Partners" as used herein shall include the general partner and the special partner as herein defined.

In Witness Whereof, the parties hereto have executed these presents as of the day and year first above written.

/s/ THOMAS HOLMES BRODHEAD,
General Partner.
/s/ MORTIMER J. GLUECK,
BISHOP TRUST COMPANY,
LIMITED
/s/ By W. A. WHITE, Its Vice Pres.,
[Seal] /s/ By E. BENNER, JR.,
Its Asst. Vice Pres.

Trustees under Deed of Trust of Thomas Holmes Brodhead, dated Sept. 30, 1942. Special Partner

Exhibit No. 2—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Mortimer J. Glueck, Co-Trustee with Bishop Trust Company, Limited, a Hawaiian corporation, under Deed of Trust, dated September 30, 1942, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed as Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Assistant

Exhibit No. 2—(Continued)

Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee with Mortimer J. Glueck, under Deed of Trust, dated September 30, 1942, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and E. Benner, Jr. acknowledged said instrument to be the free act and deed of said corporation as said Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

EXHIBIT No. 3

BILL OF SALE

This indenture, made as of the close of business on September 30, 1942, by and between Thomas Holmes Brodhead, of Honolulu, City and County of Honolulu, Territory of Hawaii, a citizen of the United States of America, hereinafter called the "Seller," and T. H. Brodhead Company, a special partnership composed of Thomas Holmes Brodhead, as general partner, and Mortimer J. Glueck, of Honolulu aforesaid, who is a citizen of the United States of America, and Bishop Trust Company, Limited, a Hawaiian corporation and a majority of whose officers and directors are citizens of the United States of America, Trustee under deed of trust dated September 30, 1942, made by Thomas Holmes Brodhead as Settlor, as Special Partner,

Exhibit No. 3—(Continued)

having its principal place of business in Honolulu aforesaid, hereinafter called the "Partnership",

Witnesseth That:

The Seller, for and in consideration of the sum of One Dollar ($1.00), lawful money of the United States of America, and other good and valuable consideration to him paid, the receipt whereof is hereby acknowledged, does hereby grant, bargain, sell, assign, transfer, set over, confirm and deliver unto the Partnership and its successors and assigns forever;

All and singular, the rights, property, assets and privileges owned by the Seller and used in the business known as "T. H Brodhead," as shown on the balance sheet prepared by Cameron & Johnstone, dated as of the close of business on September 30, 1942, a copy of which is attached hereto, incorporated herein and made a part hereof for all purposes, including particularly but not in anywise limiting the generality of the foregoing, all chattels, leaseholds, improvements, machines and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, books, accounts, inventories, together with all other personal property, goods and chattels, of every kind and description and wheresoever situate, all good will, trade names, trade connections, licenses, and all contracts and agreements, including any and all rights under policies of indemnity, fidelity or other bonds or insurance of any and every kind, or cash on hand or in bank or banks, bonds, mortgages, conditional sales agreements, accounts and bills receivable, promissory notes, claims, demands, equi-

Exhibit No. 3—(Continued)

ties and choses in action, and all other property and assets, tangible and intangible, of every kind or nature owned or claimed by the Seller and used by him in the business now carried on and shown on said balance sheet, save and except the consideration received by him from the partnership as the purchase price for the foregoing;

To have and to hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits and appurtenances to the same or any part thereof belonging or appertaining or held and enjoyed therewith, unto the Partnership, its successors and assigns, absolutely and forever or in fee simple as the case may be.

And the partnership, in consideration of the foregoing, does hereby covenant and agree that it will and by these presents does assume all of the liabilities, obligations and indebtedness of the Seller, shown on said balance sheet attached hereto, and does covenant and agree to pay and discharge the same as fully and completely as though the said liabilities, obligations and indebtedness had been incurred directly by said Partnership, and to indemnify and hold harmless the said Seller from all liability, expense or obligation upon the same or arising in connection therewith;

And for the consideration aforesaid, the Seller, for himself and his heirs, executors and administrators, does hereby irrevocably appoint the Partnership, its successors and assigns, his true and lawful attorney in his name, place and stead to ask, demand, sue for and recover any and all moneys, assets or other property conveyed and transferred

Exhibit No. 3—(Continued)

hereby or intended so to be and the rights and benefits therefor, and does further covenant that he, the Seller, will at any time at the request of the Partnership make, do execute and deliver all such receipts, powers of attorney and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property, claims and demands hereinabove conveyed and assigned or intended so to be as the Partnership reasonably may require.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

/s/ THOMAS HOLMES BRODHEAD,
Seller.
T. H. BRODHEAD COMPANY,
a Special Partnership,
/s/ By THOS. H. BRODHEAD,
General Partner,
Buyer.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Exhibit No. 3—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Thomas H. Broadhead, to me personally known, who, being by me duly sworn, did say that he is a General Partner of T. H. Brodhead Company, a special partnership; that said instrument was signed on behalf of said partnership by authority of all the partners; and that said Thos. H. Brodhead acknowledged said instrument to be the free act and deed of said partnership.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires June 30, 1945.

T. H. BRODHEAD

BALANCE SHEET AS AT SEPTEMBER 30, 1942

ASSETS

CURRENT ASSETS		
Cash in banks:		
Anglo-California National Bank	$ 5,125.73	
Bank of Hawaii	16,406.61	$ 21,532.34
Accounts receivable		64,667.35
Employment taxes receivable from employees:		
Public welfare	80.33	
Social security	79.85	160.18
Exchange account		122.92
Merchandise inventory		27,310.44
Total current assets		113,793.23

Exhibit No. 3—(Continued)

FIXED ASSETS, Schedule I			
Automobiles, at cost	$4,548.95		
Less: Depreciation reserve	2,203.28	2,345.67	
Furniture and fixtures	2,207.75		
Less: Depreciation reserve	530.33	1,677.42	4,023.09
Investment in Brodhead-Warren, Ltd.			6,100.00
Advance payments for merchandise			54,682.41
Total Assets			$178,598.73

LIABILITIES and NET WORTH

CURRENT LIABILITIES		
Account payable	$72,448.56	
Loan payable, Bank of Hawaii	9,000.00	
Taxes payable	12,900.17	
Accrued salaries payable	4,000.00	
Accrued expense	250.00	$ 98,598.73
CAPITAL		80,000.00
Total liabilities and net worth		$178,598.73

EXHIBIT No. 4

In the Office of the Treasurer of the
Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

CERTIFICATE OF SPECIAL PARTNERSHIP

The undersigned, a Special Partnership, hereby certify in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935, as follows:

1. The name under which the partnership is to be conducted is "T. H. Brodhead Co.";

2. The general nature of the business intended to be tranacted is to buy, sell, import, export, trade and deal in goods, wares and merchandise of every kind or nature and to engage in and carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers, and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places as the partners from time to time shall determine;

3. The names of the partners and the residence of each are as follows:

Thomas Holmes Brodhead, General Partner, Honolulu, T. H.

Exhibit No. 4—(Continued)

Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, as Settlor, Special Partner, Honolulu, T.H.

4. The amount of capital which the Special Partner has contributed to the special partnership assets is $40,000.00.

5. The term for which the partnership is to exist commenced on October 1, 1942, and will continue until September 30, 1952, and thereafter from year to year until terminated as provided in that certain Special Partnership Agreement dated September 30, 1942.

In Witness Whereof the undersigned have caused this certificate to be executed this 23rd day of December, 1942.

/s/ THOMAS HOLMES BRODHEAD,
General Partner
/s/ MORTIMER J. GLUECK,
BISHOP TRUST COMPANY,
LIMITED,
[Seal] /s/ By W. A. WHITE, Its Vice President
Trustees as aforesaid
Special Partner

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Thomas Holmes Brodhead, to me

Exhibit No. 4—(Continued)

personally known to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared Mortimer J. Glueck, to me known, who, being be my duly sworn, did say that he is one of the Trustees under that certain Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, as Settlor; and acknowledged that he executed the foregoing instrument as his free act and deed as said Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 23rd day of December, 1942, before me personally appeared W. A. White, to me known, who, being by me duly sworn, did say that he is the Vice President of Bishop Trust Company, Limited, a Hawaiian corporation, one of the Trustees under

Exhibit No. 4—(Continued)

that certain Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, as Settlor; that the seal affixed to the foregoing instrument is the corporate seal of said corporation; that the instrument was signed and seal in behalf of said corporation as Trustee aforesaid by authority of its Board of Directors; and the said W. A. White acknowledged said instrument to be the free act and deed of said corporation as said Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935.

Territory of Hawaii,
City and County of Honolulu—ss:

Thomas Holmes Brodhead, being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead, as Settlor, is a

Exhibit No. 4—(Continued)

Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner said Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees as aforesaid, actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money.

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ THOMAS HOLMES BRODHEAD

Subscribed and sworn to before me this 23rd day of December, 1942.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935

Teritory of Hawaii,
City and County of Honolulu—ss:

Mortimer J. Glueck, being first duly sworn, on oath doth depose and say:

That he is one of the Trustees under the Deed of

Exhibit No. 4—(Continued)

Trust dated September 30, 1942, made by Thomas Holmes Brodhead as Settlor; that he and Bishop Trust Company, Limited, a Hawaiian corporation, as Trustees under said Deed of Trust and not in their individual capacity, are a Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner they actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money.

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ MORTIMER J. GLUECK

Subscribed and sworn to before me this 23rd day of December, 1942.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Exhibit No. 4—(Continued)

In the Office of the Treasurer of the
Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935

Territory of Hawaii,
City and County of Honolulu—ss:

W. A. White, being first duly sworn, on oath doth depose and say:

That he is Vice-President of Bishop Trust Company, Limited, a Hawaiian corporation, and as such is authorized to make this Affidavit on its behalf;

That said Bishop Trust Company, Limited, is one of the Trustees under the Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead as Settlor; that said Bishop Trust Company, Limited, a Hawaiian corporation, and Mortimer J. Glueck, as Trustees under said Deed of Trust and not in their individual capacity, is a Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner said Mortimer J. Glueck and Bishop Trust Company, Limited, Trustee as aforesaid, actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money.

And further affiant sayeth not except that this

Exhibit No. 4—(Continued)

Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ W. A. WHITE

Subscribed and sworn to before me this 23rd day of December, 1942.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

EXHIBIT No. 5

(Deed of Trust—Elizabeth S. Brodhead Trust)

This Indenture, dated this 28th day of February, 1943, by and between Elizabeth S. Brodhead, who is a citizen of the United States of America, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter called the "Settlor", and Mortimer J. Glueck, of Honolulu aforesaid, who is a citizen of the United States of America, and Bishop Trust Company, Limited, a Hawaiian corporation and a majority of whose officers and directors are citizens of the United States of America, hereinafter called the "Trustees",

Witnesseth That:

The Settlor, in consideration of the love and affection she bears the beneficiaries and of the acceptance by the Trustees of the trust herein created, does hereby transfer, set over and deliver to the Trustees, their successors in trust and assigns, the sum of

Exhibit No. 5—(Continued)

Ten Thousand and no/100ths Dollars ($10,000.00);

To Have and to Hold the same, together with all other property which may hereafter be or become a part of the trust estate hereby created, unto the Trustees, their successors in trust and assigns, in trust nevertheless for the uses and purposes hereinafter stated, that is to say:

(a) The Trustees shall purchase the fifty per cent (50%) capital interest of the special partner in the partnership known as "T. H. Brodhead Co.", a special partnership duly organized and operating under that certain Special Partnership Agreement dated September 30, 1942, paying $40,000.00 therefor, said amount being the fair and reasonable value of said interest duly ascertained as of February 28, 1943, and the Trustees shall pay $10,000.00 cash therefor and agree to pay the balance of the purchase price out of the assets of the trust estate, upon such terms and conditions as the Trustees may deem advisable, and shall become and continue to be a special partner therein;

(b) The Trustees shall accumulate all income from the said trust estate during the continuance thereof, and except as hereinafter provided, all of said net income shall be added to and become a part of the corpus of the trust estate and be invested and reinvested as a part of said corpus during the existence of this trust;

(c) The Trustees shall pay one-half (½) of the accumulated net income from said trust estate in equal shares to the children of the Settlor then

Exhibit No. 5—(Continued)

living, but not in excess of the sum of $10,000.00 to each of said children at the time that the youngest child of the Settlor then living attains the age of twenty-three (23) years, and shall pay all of the accumulated net income from said trust estate in equal shares to the children of the Settlor then living, but not in excess of the sum of $10,000.00 to each of said children at the time that the youngest child of the Settlor then living attains the age of twenty-eight (28) years, Provided, However, that in the event that there is not sufficient cash included in the assets of said trust estate at the time that such payments become due and payable the Trustees may satisfy the obligation herein provided by transfer, assigning, and setting over to the said children of the Settlor the right of the Trustees to receive any sums of money that may be due to them as a special partner from the partnership of T. H. Brodhead Co., or any other asset owned by them as such Trustees;

(d) This trust shall cease and determine at the time that the youngest child of the Settlor attains the age of thirty-three (33) years (or would have attained such age if living) and the Trustees shall thereupon transfer, set over and deliver all the property then comprising the trust estate, together with all accumulated income thereof, absolutely and free and clear of any trusts in equal shares to the children of the Settlor then surviving and the lawful issue of any of said children who may have predeceased the Settlor (said issue to take per stirpes

Exhibit No. 5—(Continued)

and not per capita), and if there be no children or lawful issue of the Settlor her surviving, then to those persons other than the Settlor and Thomas H. Brodhead, husband of the Settlor, who would be the heirs-at-law of the last surviving of the children of the Settlor under the statutes of descent of the Territory of Hawaii in force and effect at the time of his or her death, the same as if he or she had died intestate at that time; Provided, However, that if not terminated prior thereto, the Trustees may determine this trust at any time (but not more than one (1) year) which to the Trustees may seem best after the Trustees shall cease to be a special partner in the partnership known as "T. H. Brodhead Co.";

(e) The Trustees shall receive, hold, manage and control the said trust estate, collect the income therefrom and pay all charges incident to trust estates and properly payable by said trust estate therefrom; and the Settlor authorized the Trustees to retain either permanently or temporarily or for such period of time as they may deem expedient any property conveyed, assigned or delivered to the Trustees by the Settlor of whatever nature; and the Settlor directs that the said Trustees shall not be held liable for any loss resulting to said trust estate by reason of the Trustees' retaining any such property or for any error of judgment in this respect;

(f) The Settlor authorizes and empowers the Trustees to sell at public or private sale, convert,

Exhibit No. 5—(Continued)

transfer, exchange, mortgage, hypothecate and otherwise deal in or dispose of the whole or any part of the property, real, personal and mixed, which may be from time to time a part of the trust estate, with power to accept any purchase money mortgage or mortgages for any part of the purchase or exchange price; to invest and reinvest the whole or any part of the assets of the said trust estate, and in investing and reinvesting any assets of said trust estate the Trustees may invest in common or preferred stocks of corporations, bonds, notes, debentures, participation or investment certificates and/or in any other property, real or personal, in so far as in their judgment they shall deem such investments advisable, it being the intention of the Settlor, under the foregoing provisions, to grant to the Trustees full power to invest and reinvest money in such investments as they shall deem desirable and suitable investments for trust funds without being restricted to the classes of investments which trustees are permitted by law to make; Provided, However, that the Trustees shall obtain the consent of the Settlor to make such investments during her lifetime, and Provided Further, that in the event the Settlor shall die before the termination hereof, the Trustees shall thereafter be restricted in the making of investments of trust funds to the classes of investments which trustees are permitted by law to make, except that in any event the Trustees may, without liability for any losses resulting therefrom, continue to make payments on account of its pur-

Exhibit No. 5—(Continued)

chase of its interest in or make advances or loans to the partnership known as "T. H. Brodhead Co.", its successors and assigns; the Settlor authorizes and empowers the Trustees, upon any increase of the capital stock of any corporation in which said trust estate shall own shares, to exercise any pre-emptive rights to such shares to which said trust estate may be entitled and/or to subscribe for such additional shares as in the judgment of the Trustees shall be an advisable investment; and for this purpose and for other purposes of this trust, the Settlor authorizes and empowers the Trustees to borrow money either from themselves or from others and upon such terms and conditions as they may deem appropriate; the Trustees shall have the right and power to vote either directly or by proxy the stock of any corporation that may be a part of said trust estate from time to time at all meetings of stockholders as the Trustees may deem best;

(g) Stock dividends shall be treated as capital of the trust estate and all stock acquired by the Trustees under the exercise of rights to subscribe or the net proceeds realized by the Trustees from the sale of rights to subscribe shall be treated as capital of the trust estate and all other corporate distributions shall be treated as income; Provided, However, that where a distribution is made through the reduction of any corporate stock held by the Trustees, or, in the exclusive discretion of the Trustees it appears to be made in or as a result of a partial or complete liquidation or dissolution of the

Exhibit No. 5—(Continued)

corporation, the Trustees may in their discretion make such apportionment of any such distribution between income and capital as to them may seem just; the Trustees shall have full power and authority to decide and determine in all doubtful cases what property or moneys received by them is capital and what is income; and also in doubtful cases to decide and determine what expenses and other charges are payable out of income and what out of capital; and also in all doubtful cases to decide and determine what proportion of payments for expenses of or charges against the trust estate are payable from income and what from capital; and all beneficiaries shall be bound by the decision and determination of the Trustees in regard to all such allocations between capital and income; the Trustees shall have authority in and discretion to prorate during the year and withhold from the income received by the trust estate an amount sufficient to pay proportionate shares of the expenses payable by the trust estate so that said payments of net income may be more regular and even in amount, and to withhold such amounts of income and/or principal as they may deem necessary to protect themselves from any possible liability for taxes and/or costs or expenses in connection with or arising out of possible claims therefor;

(h) The Settlor may transfer, convey and assign to the Trustees any property in addition to that hereinbefore referred to, to be held upon the trust hereby created, and thereafter such additional prop-

Exhibit No. 5—(Continued)

erty shall be and form a part of the trust estate;

(i) The Trustees shall render annual statements of account to the persons who are the beneficiaries of this trust, as hereinabove provided, but the Trustees shall not be required to account in any court unless requested so to do by a beneficiary; Provided, However, that the Trustees may whenever they shall deem it advisable file accounts in any court having jurisdiction thereof for approval, the costs of said proceedings to be paid out of the trust estate;

(j) If any person entitled to receive any of the income and/or capital of the trust estate shall be a minor, the Trustees may pay the share of income and/or capital to which said minor is entitled to either parent of or to the natural or legally appointed guardian of such minor, and the receipt of such parent or natural or legally appointed guardian shall be a complete release, discharge and acquittance of the Trustees to account further for any payment or payments so made, and if any beneficiary is a minor, the statements of account may be furnished to either parent of or to the natural or legally appointed guardian of such minor beneficiary;

(k) Bishop Trust Company, Limited, the corporate Trustee hereunder, shall have the custody and safekeeping of all moneys and securities belonging to the trust estate which are received or collected by the Trustees. Neither Trustee hereunder shall

Exhibit No. 5—(Continued)

be answerable or accountable for any act of the other Trustee in which he or it shall not participate, nor for the custody of any property except as shall come to his or its own possession or personal control, nor for any loss or damage resulting from any error of judgment or otherwise except through his or its own gross neglect or wilful default. Nor shall the Trustees or either of them be answerable or accountable for any loss or damage resulting from any act consented to by the Settlor or for any loss or damage resulting from any investment in or loan or advance to the partnership of "T. H. Brodhead Co.", its successors and assigns;

(l) No beneficiary hereunder shall have the power or authority to anticipate in anywise any of the rents, issues, profits, income, moneys or payments herein provided to be devoted or paid to him or her or any part thereof, nor to alienate, encumber, convey, transfer or dispose of the same or of any interest therein or part thereof, in advance of payment; nor shall the same be involuntarily alienated by him or her or be subject to attachment or execution or be levied upon or taken upon any process for any debts which any such beneficiary shall have contracted or in satisfaction of any demands or obligations which he or she shall incur. All payments or distribution of either income and/or principal as hereinabove provided shall be made by the Trustees and subject to the provisions of subparagraph (j) hereinabove shall be valid and effectual only when made to the beneficiary to whom the

Exhibit No. 5—(Continued)

same shall appertain and belong, and upon his or her individual receipt; Provided, However, that when and while the person so entitled to receive such payment shall be without the bounds of the Territory of Hawaii, such payment may be made to any formally appointed agent of such person, but only upon the personal receipt above provided for;

(m) In the event that Mortimer J. Glueck shall be or become unable to act or shall decline to act or shall resign his office as Co-trustee hereunder, or from and after the death of Mortimer J. Glueck prior to the termination of this trust, then and in any of such events, Edouard R. L. Doty shall be substituted as Co-trustee in his place and stead and in the event that Edouard R. L. Doty shall be or become unable to act or shall decline to act or shall resign his office as Co-trustee hereunder or from and after the death of Edouard R. L. Doty prior to the termination of the trust, Bishop Trust Company, Limited, may select some person to be substituted as Trustee in the place and stead of said Edouard R. L. Doty, and title to all property then comprising the trust estate shall be vested in such person and Bishop Trust Company, Limited, as Trustees without any conveyance or vesting order;

(n) It is hereby declared that this agreement shall be and is hereby made irrevocable by the Settlor and the Settlor reserves the right to amend this instrument only by adding other property to be and become a part of the estate held under the terms hereof, and the right to alter, amend, cancel

Exhibit No. 5—(Continued)

or revoke any provisions of this instrument, save and except paragraphs (a), (b), (c), and (d) hereof; Provided, However, that in no event shall any of the property or the income thereof belonging to the trust estate be paid to or inure to the benefit of the Settlor, and Provided Further, that any amendments made by the Settlor shall be made by instrument in writing and acknowledged and filed with the Trustees, and that the alteration, amendment, cancellation or revocation of any provision of this instrument shall be made only with the written consent and approval of the Trustees and of all the beneficiaries hereunder;

The said Mortimer J. Glueck and Bishop Trust Company, Limited, hereby accept the within trust and covenants and agree with the Settlor that they will faithfully discharge and carry out the same.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

/s/ ELIZABETH S. BRODHEAD,
Settlor

/s/ MORTIMER J. GLUECK,
BISHOP TRUST COMPANY,
LIMITED

[Seal] /s/ By W. A. WHITE,
Its Vice President

/s/ By G. W. FISHER,
Its Asst. V.P.
Trustees

Exhibit No. 5—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 3rd day of May, 1943, before me personally appeared Elizabeth S. Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that she executed the same as her free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 3rd day of May, 1943, before me personally appeared Mortimer J. Glueck, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 4th day of May, 1943, before me appeared W. A. White and G. W. Fisher, to me personally known, who, being by me duly sworn, did say that they are the Vice President and Asst. Vice Pres., respectively, of Bishop Trust Company, Limited,

Exhibit No. 5—(Continued)

a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and G. W. Fisher acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

EXHIBIT No. 6

ASSIGNMENT

This Indenture, made this 28th day of February, 1943, by and between Mortimer J. Glueck, of Honolulu, City and County of Honolulu, Territory of Hawaii, who is a citizen of the United States of America, and Bishop Trust Company, Limited, a Hawaiian corporation, a majority of whose officers and directors are citizens of the United States of America, Trustees under Deed of Trust of Thomas Holmes Brodhead, dated September 30, 1942, hereinafter called the "Assignors", and Mortimer J. Glueck, of Honolulu aforesaid, who is a citizen of the United States of America, and Bishop Trust Company, Limited, a Hawaiian corporation, a majority of whose officers and directors are citizens of the United States of America as aforesaid, Trus-

Exhibit No. 6—(Continued)

tees under Deed of Trust of Elizabeth S. Brodhead, dated February 28, 1943, hereinafter called the "Assignees",

Witnesseth That:

The Assignors, for and in consideration of the sum of Ten Thousand and No/100ths Dollars ($10,000.00), lawful money of the United States of America, and other good and valuable consideration to them paid, the receipt of which is hereby acknowledged, do hereby assign, transfer, set over, and deliver unto the Assignees, their successors and assigns in trust, all of their right, title and interest in and to their fifty per cent (50%) capital interest of the special partnership known as "T. H. Brodhead Co.", a partnership duly organized and operating under that certain Special Partnership Agreement dated September 30, 1942, Provided, However, that nothing herein contained shall constitute an assignment of any of their right to the advance account covering the share of the Assignors in the undivided profits of said special partnership to February 28, 1943.

To Have and to Hold the same unto the Assignees, their successors and assigns in trust, absolutely.

And Thomas Holmes Brodhead, who is a citizen of the United States of America, of Honolulu aforesaid, being the General Partner in said Special Partnership known as "T. H. Brodhead Co,", hereby consents to the assignment of said partnership interest as herein provided.

In Witness Whereof, the parties hereto have exe-

Exhibit No. 6—(Continued)

cuted these presents as of the day and year first above written.

/s/ MORTIMER J. GLUECK, and
[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustees under Deed of Trust of Thomas Holmes Brodhead, dated September 30, 1942, and not individually.

/s/ By W. A. WHITE, Its Vice Pres.,
/s/ By G. W. FISHER, Its Asst. V.P.
/s/ THOMAS HOLMES BRODHEAD

Territory of Hawaii,
City and County of Honolulu—ss:

On this 3rd day of May, 1943, personally appeared before me Thomas Holmes Brodhead, known to me to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On the 3rd day of May, 1943, before me personally appeared Mortimer J. Glueck, Co-Trustee with Bishop Trust Company, Limited, a Hawaiian corporation, under Deed of Trust of Thomas Holmes

Exhibit No. 6—(Continued)

Brodhead, dated September 30, 1942, to me known to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed as said Co-trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 4th day of May, 1943, before me appeared W. A. White and G. W. Fisher, to me personally known, who, being by me duly sworn, did say that they are the Vice President and the Assistant Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee with Mortimer J. Glueck under Deed of Trust of Thomas Holmes Brodhead, dated September 30, 1942, and that the seal affixed to said instrument is the corporate seal of said corporation and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and G. W. Fisher acknowledged said instrument to be the free act and deed of said corporation as said Co-trustee.

[Seal] FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

EXHIBIT No. 7

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

CERTIFICATE OF CHANGE OF SPECIAL PARTNERSHIP

The undersigned, a Special Partnership, hereby certify in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935, as follows:

1. The name under which the partnership is to be conducted is "T. H. Brodhead Co.";

2. The general nature of the business intended to be transacted is to buy, sell, import, export, trade and deal in goods, wares and merchandise of every kind or nature and to engage in and carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers, and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at 843 Kaahumanu Street, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places as the partners from time to time shall determine;

3. The names of the partners and the residence of each are as follows:

Exhibit No. 7—(Continued)

Thomas Holmes Brodhead, General Partner, Honolulu, T.H.

Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Elizabeth S. Brodhead, dated February 28, 1943, Special Partner, Honolulu, T.H.

Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Thomas Holmes Brodhead, dated September 30, 1942, have withdrawn from the Special Partnership;

4. The amount of capital which the Special Partner has contributed to the partnership assets is $40,000.00.

5. The change in the Special Partnership became effective on February 28, 1943. The Special Partnership will continue until September 30, 1952, and thereafter from year to year until terminated as provided in that certain Special Partnership Agreement dated September 30, 1942.

In Witness Whereof, the undersigned have caused this certificate to be executed this 3rd day of May, 1943.

/s/ THOMAS HOLMES BRODHEAD,
/s/ MORTIMER J. GLUECK, and
[Seal] BISHOP TRUST COMPANY,
LIMITED,
Trustees as aforesaid.

/s/ By W. A. WHITE, Its Vice Pres.,
/s/ By G. W. FISHER, Ist Asst. V.P.

Exhibit No. 7—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 3rd day of May, 1943, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 3rd day of May, 1943, before me personally appeared Mortimer J. Glueck, Co-trustee with Bishop Trust Company, Limited, a Hawaiian corporation, under Deed of Trust of Elizabeth S. Brodhead, dated February 28, 1943, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed as said Co-trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 4th day of May, 1943, before me appeared W. A. White and G. W. Fisher, to me personally

Exhibit No. 7—(Continued)

known, who, being by me duly sworn, did say that they are the Vice President and Asst. Vice Pres., respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-trustee with Mortimer J. Glueck under Deed of Trust of Elizabeth S. Brodhead, dated February 28, 1943, and that the seal affixed to said instrument is the corporate seal of said corporation and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and G. W. Fisher acknowledged said instrument to be the free act and deed of said corporation as said Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935

Territory of Hawaii,
City and County of Honolulu—ss:

Thomas Holmes Brodhead, being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and

Exhibit No. 7—(Continued)

County of Honolulu, Territory of Hawaii; that Mortimer J. Glueck and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor, are a Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner said Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees as aforesaid, actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ THOMAS HOLMES BRODHEAD

Subscribed and sworn to before me this 3rd day of May, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

Exhibit No. 7—(Continued)

In the Office of the Treasurer of the
Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935

Territory of Hawaii,
City and County of Honolulu—ss:

Mortimer J. Glueck, being first duly sworn, on oath doth depose and say:

That he is one of the Trustees under the Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor; that he and Bishop Trust Company, Limited, a Hawaiian corporation, as Trustees under said Deed of Trust and not in their individual capacity, are a Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner they actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money.

And further affiant sayest not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ MORTIMER J. GLUECK

Exhibit No. 7—(Continued)

Subscribed and sworn to before me this 3rd day of May, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of T. H. BRODHEAD CO.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII 1935

Territory of Hawaii,
City and County of Honolulu—ss:

W. A. White, being first duly sworn, on oath doth depose and say:

That he is Vice-President of Bishop Trust Company, Limited, a Hawaiian corporation, and as such is authorized to make this Affidavit on its behalf;

That said Bishop Trust Company, Limited, is one of the Trustees under the Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor; that said Bishop Trust Company, Limited, a Hawaiian corporation, and Mortimer J. Glueck, as Trustees under said Deed of Trust and not in their individual capacity, is a Special Partner in the partnership of T. H. Brodhead Co.; that as Special Partner said Mortimer J. Glueck and

Exhibit No. 7—(Continued)

Bishop Trust Company, Limited, Trustees as aforesaid, actually have paid into the partnership as a capital contribution the sum of $40,000.00 in lawful money.

And further affiant sayeth not except that this affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ W. A. WHITE

Subscribed and sworn to before me this 4th day of May, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My commission expires June 30, 1945.

EXHIBIT No. 8

AMENDMENT OF SPECIAL PARTNERSHIP AGREEMENT

This Agreement, dated as of the close of business on the 28th day of February, 1947, made by and between Thomas Holmes Brodhead, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter referred to as "General Partner", and Mortimer J. Glueck, of Honolulu aforesaid, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor, hereinafter referred to as "Special Partner",

Exhibit No. 8—(Continued)

Witnesseth That:

Whereas said Thomas Holmes Brodhead, General Partner, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead as Settlor, Special Partner, did form a Special Partnership known as "T. H. Brodhead Co.", by a special partnership agreement dated as of the 30th day of September, 1942; and,

Whereas said Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Thomas Holmes Brodhead dated September 30, 1942, did assign their interest in said special partnership known as "T. H. Brodhead Co." to Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Elizabeth S. Brodhead dated February 28, 1943, by Assignment dated the 28th day of February, 1943; and,

Whereas the parties hereto are desirous of changing the name of said partnership from "T. H. Brodhead Co." to "Ace Distributors",

Now, Therefore, This Indenture Further Witnesseth That:

That certain partnership agreement dated as of the 30th day of September, 1942, made by and bebetween Thomas Holmes Brodhead, General Partner, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated September 30, 1942, made by Thomas Holmes Brodhead as Settlor, Special Partner, is hereby amended as follows:

Exhibit No. 8—(Continued)

Paragraph 2 thereof shall be and the same is hereby amended to read as follows:

"2. Name: The partnership shall be conducted and carried on under the firm name and style of 'Ace Distributors', and the place or places of business shall be at Honolulu aforesaid, and/or at such other place or places as the partners may from time to time determine."

In Witness Whereof, the parties hereto have executed these presents as of the day and year first above written.

/s/ THOMAS HOLMES BRODHEAD,
General Partner.

/s/ MORTIMER J. GLUECK and
[Seal] BISHOP TRUST COMPANY,
LIMITED, Trustees as aforesaid

/s/ By E. BENNER, JR., Its Vice Pres.,
/s/ By G. W. FISHER, Its Vice Pres.
Special Partner

Territory of Hawaii,
City and County of Honolulu—ss:

On this 4th day of April, 1947, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

Exhibit No. 8—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 4th day of April, 1947, before me personally appeared Mortimer J. Glueck, Co-Trustee with Bishop Trust Company, Limited, a Hawaiian corporation, under Deed of Trust of Elizabeth S. Brodhead dated February 28, 1943, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed as said Co-Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 28th day of February, 1947, before me appeared E. Benner, Jr., and G. W. Fisher, to me personally known, who, being by me duly sworn, did say that they are the Vice-President and Vice-President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Co-Trustee with Mortimer J. Glueck under Deed of Trust of Elizabeth S. Brodhead dated February 28, 1943, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that the said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr. and G.

Exhibit No. 8—(Continued)

W. Fisher acknowledged said instrument to be the free act and deed of said corporation as said Co-Trustee.

[Seal] MARTHA M. FOWLER,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires May 17, 1948.

EXHIBIT No. 9

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Special Partnership of Ace Distributors (formerly T. H. Brodhead Co.).

CERTIFICATE OF CHANGE OF SPECIAL PARTNERSHIP

The undersigned, a Special Partnership, hereby certifies in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935, as follows:

1. The name under which the partnership is to be conducted is "Ace Distributors", the name having been changed from T. H. Brodhead Co., as of the close of business on February 28, 1947.

2. The general nature of the business intended to be transacted is to buy, sell, import, export, trade and deal in goods, wares and merchandise of every kind or nature and to engage in and carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers, and such other business as may be necessary, suit-

Exhibit No. 9—(Continued)

able or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at 843 Kaahumanu Street, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places as the partners from time to time shall determine.

3. The names of the partners and the residence of each are as follows:

Thomas Holmes Brodhead, General Partner, Honolulu, T. H.

Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust of Elizabeth S. Brodhead, dated February 28, 1943. Special Partner, Honolulu, T. H.

4. The amount of capital which the Special Partner has contributed to the partnership assets is $40,000.00.

5. The change in the Special Partnership became effective on February 28, 1947. The Special Partnership will continue until September 30, 1952, and thereafter from year to year until terminated as provided in that certain Special Partnership Agreement dated September 30, 1942.

In witness whereof, the undersigned has caused this certificate to be executed this 27th day of February, 1947.

/s/ THOMAS HOLMES BRODHEAD

Exhibit No. 9—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 27th day of February, 1947, before me personally appeared Thomas Holmes Brodhead, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

EXHIBIT No. 10

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of the Incorporation of T. H. BRODHEAD CO., LTD.

AFFIDAVIT OF OFFICERS

Territory of Hawaii,
City and County of Honolulu—ss:

Thomas H. Brodhead, Theresa S. Beerman, and Elizabeth S. Brodhead, being first duly sworn, each for himself or herself on oath deposes and says:

That Thomas H. Brodhead is the President, Theresa S. Beerman is the Treasurer, and Elizabeth S. Brodhead is the Secretary of T. H. Brodhead Co., Ltd.; that the Articles of Association of said T. H. Brodhead Co., Ltd., have been adopted, executed and

Exhibit No. 10—(Continued)

authorized by the incorporators of said corporation, and the same are ordered to be filed in the Office of the Treasurer of the Territory of Hawaii;

That the number of authorized shares of capital stock of said corporation is ten thousand (10,000) shares of common stock of the par value of Ten Dollars ($10.00) each, and the subscription price subscribed for by each subscriber is Ten Dollars ($10.00) for each share of common stock subscribed by the subscribers;

That the amount of the capital stock of said corporation is One Hundred Thousand Dollars ($100,000.00), with the privilege of subsequent increase or extension of said capital stock to an amount not exceeding One Million Dollars ($1,000,000.00);

That the names of the subscribers of said capital stock, together with the number of shares subscribed by each and the amount of capital paid in by each subscriber are as follows:

Names of Subscribers	No. of Shares	Subscription Price	Amount Paid In
Thomas Holmes Brodhead.....	4,000	$40,000.00	$40,000.00
Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor	4,000	40,000.00	40,000.00
	8,000	$80,000.00	$80,000.00

That Thomas Holmes Brodhead, General Partner, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead

Exhibit No. 10—(Continued)

as Settlor, Special Partner, are the owners of that certain business known as Ace Distributors (formerly T. H. Brodhead Co.); that certain property and assets owned by them and used in the operation of said business are to be conveyed to T. H. Brodhead Co., Ltd., as of the close of business on February 28, 1947, by form of conveyance and agreement annexed hereto and marked "Exhibit A" which will be supplemented by such additional instruments of further assurance and for the conveying of title to specific assets as may be advised by counsel in the premises to the end that the property and assets of said Ace Distributors shown on the balance sheet attached to the aforesaid conveyance and agreement shall be conveyed to said corporation.

That in and by said conveyance and agreement it is made to appear that T. H. Brodhead Co., Ltd., is to issue as fully paid up capital stock, shares of common stock in the amount of $40,000.00 to Thomas Holmes Brodhead, and in the amount of $40,000.00 to Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees as aforesaid, a total amount of $80,000.00, which amount shall be equal to the book value of the property and assets conveyed, less certain liabilities in connection therewith, which T. H. Brodhead Co., Ltd., assumes and agrees to pay (which amount is hereinafter referred to as the "net book value"); Provided, However, that the partners of Ace Distributors shall pay to the corporation such additional amount in cash which when added to their respective shares of the net book value shall be equivalent to the par value of the stock subscribed by each of said partners, and so

Exhibit No. 10—(Continued)

that the aggregate of the net book value so paid in shall total $80,000.00; that affiants are fully familiar with said assets and businesses and that said assets and businesses have a market value equal to the book value thereof.

That the sum of Eighty Thousand and No/100ths Dollars ($80,000.00) in lawful money of the United States of America and in property as aforesaid has been paid in to said corporation as payment in full of subscriptions to the capital stock of said corporation having a total par value of $80,000.00.

Subscribed and sworn to before me this 27th day of February, 1947.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

/s/ THOMAS H. BRODHEAD,
/s/ THERESA S. BEERMAN,
/s/ ELIZABETH S. BRODHEAD.

"EXHIBIT A"

BILL OF SALE

This Indenture, made as of the close of business on February 28, 1947, by and between Ace Distributors (formerly T. H. Brodhead Co.), a Special Partnership, duly registered in the Office of the Treasurer of the Territory of Hawaii, composed of Thomas Holmes Brodhead, General Partner, and Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as

Exhibit No. 10—(Continued)

Settlor, Special Partner, hereinafter called the "Seller", and T. H. Brodhead Co., Ltd., a Hawaiian corporation, hereinafter called the "Purchaser",

Witnesseth That:

Whereas the Seller is the owner of that certain business conducted under the name of Ace Distributors (formerly T. H. Brodhead Co.); and,

Whereas the members of the Seller have subscribed for eight thousand (8,000) shares of the capital stock of the Purchaser and have agreed to pay in full for said shares the total par value thereof, or Eighty Thousand and No/100ths Dollars ($80,000.00) by conveying to the Purchaser certain assets and property owned by the Seller and used in the business now carried on by it, and paying cash in addition, if necessary, which together have a market value of $80,000.00, upon the promises, terms, agreements, conditions and provisos as are hereinafter more fully set forth;

Now, therefore, this conveyance and agreement further witnesseth that:

The Seller, for and in consideration of the issuance by the Purchaser of 8,000 fully paid shares of its, the Purchaser's capital stock, having a par value of $80,000.00, to the members of the Seller, as follows:

Name	Number of Shares
Thomas Holmes Brodhead	4,000
Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor	4,000

Exhibit No. 10—(Continued)

does hereby grant, bargain, sell, assign, transfer, set over, confirm and deliver unto the Purchaser and its successors and assigns forever:

All those certain rights, property, assets and privileges owned by the Seller and used in the business known as "Ace Distributors" (formerly "T. H. Brodhead Co."), as shown on the balance sheet prepared by Cameron & Johnstone, dated as of the 28th day of February, 1947, a copy of which is attached hereto, incorporated herein and made a part hereof for all purposes, and subject to the liabilities, obligations and indebtedness shown on said balance sheet.

To have and to hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits, and appurtenances to the same or any part thereof belonging or appertaining or held and enjoyed therewith, unto the Purchaser, its successors and assigns, absolutely and forever, or in fee simple, as the case may be.

And the Purchaser, in consideration of the foregoing, does hereby covenant and agree that it will, and by these presents does assume the liabilities, obligations and indebtedness of the Seller which are shown on the aforesaid balance sheet and does covenant and agree to pay and discharge the same as fully and completely as through the said liabilities, obligations and indebtedness had been incurred directly by said Purchaser, and to idemnify and hold harmless the said Seller from all liability, expense or obligations upon the same or arising in connection therewith;

And for the consideration aforesaid, the Seller,

Exhibit No. 10—(Continued)

for itself and its successors and assigns, does hereby irrevocably appoint the Purchaser, its successors and assigns, its true and lawful attorney, in its name, place and stead, to ask, demand, sue for and recover any and all moneys, assets or other property conveyed and transferred hereby or intended so to be and the rights and benefits therefor, and does further covenant that it, the Seller, will at any time at the request of the Purchaser, make, do, execute and deliver all such receipts, powers of attorney and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property, claims and demands hereinabove conveyed and assigned, or intended so to be, as the Purchaser reasonably may require;

And, as consideration for the conveyance and promises as aforesaid, the Purchaser for itself and its successors and assigns hereby covenants, promises and agrees to and with the Seller, and the members thereof, and their respective heirs, executors, administrators, successors in trust and assigns, to issue to and in the name of and deliver to the members of the Seller, certificates for fully paid shares of the common capital stock of the Purchaser as follows:

Name	Number of Shares
Thomas Holmes Brodhead	4,000
Mortimer J. Glueck and Bishop Trust Company, Limited, Trustees under Deed of Trust dated February 28, 1943, made by Elizabeth S. Brodhead as Settlor	4,000

Exhibit No. 10—(Continued)

the total of said shares to be equal to the book value of the assets and businesses so conveyed, less all of the liabilities thereof or pertaining thereto, or in connection therewith, which the Purchaser has hereinbefore assumed and promises to pay (which amount is hereinafter referred to as the "net book value"); Provided, However, that the Seller and the members thereof shall pay to the Purchaser such additional amount in cash which when added to their respective shares of the net book value shall be equivalent to the par value of the stock subscribed by each of said members and so that the aggregate of the net book value and the cash so paid in shall total $80,000.00.

In Witness Whereof, the parties hereto have executed these presents as of the day and year first above written.

ACE DISTRIBUTORS

/s/ By THOMAS HOLMES BRODHEAD,
General Partner.
Seller,

T. H. BRODHEAD CO., LTD.

/s/ By THOS. H. BRODHEAD,
Its President.

/s/ By THERESA S. BEERMAN,
Its Treasurer.

Exhibit No. 10—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss:

On this 27th day of February, 1947, before me appeared Thomas Holmes Brodhead, to me personally known, who, being by me duly sworn, did say that he is the General Partner of Ace Distributors, a special partnership organized and doing business in the Territory of Hawaii, and as such General Partner has authority to execute the said instrument on behalf of said special partnership and the said Thomas Holmes Brodhead acknowledged said instrument to be the free act and deed of said special partnership.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

Territory of Hawaii,
City and County of Honolulu—ss:

On this 27th day of February, 1947, before me personally appeared Thomas Holmes Brodhead and Theresa S. Beerman, to me personally known, who, being by me duly sworn, did say that they are the President and Treasurer, respectively, of T. H. Brodhead Co., Ltd., a Hawaiian corporation; that the seal affixed to the foregoing instrument is the

Exhibit No. 10—(Continued)

corporate seal of said corporation; and that the foregoing instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors; and the said Thomas Holmes Brodhead and Theresa S. Beerman acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of Hawaii. My Commission expires 6-30-49.

Schedule of Income and Expenses
[illegible] 19, 19[illegible] to September 30, 1950 Inclusive

	Fiscal Year Ending September 30,								
	1943	1944	1945	1946	1947	1948	1949	1950	Total
Income									
Distributive share of income from T. H. Brodhead Co.	$36,681.45								
Interest received on notes		$2,000.00	$ 2,000.00	$1,733.47	$1,500.00	$1,000.00	$1,410.75		
Interest received on bonds and savings		125.00	125.00	250.00	350.00	450.00	475.00	$ 735.23	
Dividends received on stocks		261.75	628.50	1,259.95	1,971.70	2,223.10	2,536.57	2,870.01	
Commission refund			66.81						
Proceeds from sale of stock rights						33.42			
Partnership profits of 2/28/43, overcredited			(2,426.52)						
	$36,681.45	$2,386.75	$ 393.79	$3,263.42	$3,821.70	$3,706.52	$4,422.32	$3,605.24	$58,281.19
Expenses									
Trustee fees	366.81	170.00	249.82	258.44	293.13	287.12	337.88	280.24	
Tax service fees		15.00	25.00	25.00		25.00	25.00	35.00	
Federal income taxes			394.44	669.36	577.35	653.68	553.66	696.98	
Territorial income taxes			16.30	15.84		17.04	1.34	21.27	
Territorial C and D taxes on mainland dividends			11.10	23.34	28.21	38.24	44.54	45.29	
Interest accrued on U. S. Treasury Bonds purchased					62.64		24.05	30.33	
Bank charges and postage		.05	.20	.15	.05			.31	
Refund of overpayment of partnership profits			5,043.02						
	366.81	185.05	5,739.88	992.13	961.38	1,021.08	986.47	1,109.42	11,362.22
Net Income	$36,314.64	$2,201.70	$(5,346.09)	$2,271.29	$2,860.32	$2,685.44	$3,435.85	$2,495.82	46,918.97
Gift by Thomas H. Brodhead at September 30, 1942									40,000.00
Trust balance - Inventory attached									$86,918.97

THOMAS H. BRODHEAD TRUST

Inventory of Assets
September 30, 1950

Cash				$ 2,109.48
Stocks				
90	Shares	American Chicle Co.	$ 3,852.50	
205	"	American Factors, Ltd.	5,081.75	
120	"	Columbian Carbon Corp.	3,751.47	
111	"	Standard Oil of California	3,698.80	
75	"	F. E. Woolworth Co.	3,317.50	
139	"	Eastman Kodak Co.	4,236.26	
120	"	Pittsburg Plate Glass	3,574.32	
200	"	Hawaiian Electric Co., 4½ Pfd.	3,960.50	
110	"	Consolidated Edison Co. of New York	3,661.61	
140	"	Union Oil	3,551.31	
82	"	Continental Insurance Co.	3,324.17	
400	"	Mutual Telephone Co., Pfd.	4,082.60	
100	"	Southern California Edison	3,492.00	
50	"	Bank of Hawaii	1,871.75	51,456.54
Bonds				
U. S. Savings Bonds - Series G			10,000.00	
U. S. Treasury Bonds - 2½%			13,452.95	23,452.95
Savings and Loan Certificates				
First Federal Savings and Loan			4,900.00	
Home Mutual Savings & Loan			5,000.00	9,900.00
				$86,918.97

Exhibit 19

Schedule of Income and Expenses
February 28, 1943 to February 28, 1951 Inclusive

	Calendar Year			Fiscal Year Ending September 30,				5 Month Period Ending February 28,	
	1944	1945	1946	1947	1948	1949	1950	1951	Total
Income									
Distributive share of profits and (losses) of T. H. Brodhead Co. for fiscal year ending February 28	$40,537.19	$65,202.78	$57,847.70	$ 379.23					
Distributive share of profits and (losses) of Ace Distributors for fiscal year ending February 28					$ (3,814.88)	$14,054.66	$ (67.08)	$1,882.80	
Adjustment of gross income tax of T. H. Brodhead Co., for fiscal year ended February 28, 1944		1,205.18							
Interest								58.68	
Dividends								24.50	
	$40,537.19	$66,407.96	$57,847.70	$ 379.23	$(3,814.88)	$14,054.66	$ (67.08)	$1,965.98	$177,210.76
Expenses									
Interest	$ 1,500.00	$ 1,500.00	$ 1,253.47	$ 1,000.00	$ 1,000.00	$ 1,410.75			
Trustee fees			1,647.93	300.00	300.00	300.00	$ 300.00	$ 300.00	
Tax service fee	15.00	25.00	25.00	25.00	15.00	15.00	15.00	15.00	
Federal income taxes		19,912.09	38,737.09	21,279.33	7,093.09		46.31		
Territorial income taxes		1,149.83	2,105.92	350.92					
Notary fees					.50		.50		
	$ 1,515.00	$22,586.92	$43,769.41	$22,955.25	$ 8,408.59	$ 1,725.75	$ 361.81	$ 315.00	$101,637.73
Net income	$39,022.19	$43,821.04	$14,078.29	$(22,576.02)	$(12,223.47)	$12,328.91	$(428.89)	$1,650.98	$ 75,673.03
Gift by Thomas H. Brodhead at February 28, 1943									10,000.00
Trust balance - Inventory attached									$ 85,673.03

ELIZABETH S. BRODHEAD TRUST

Schedule of Receipts of Distributive Share of Income From T. H. Brodhead Co. and Ace Distributors

	Calendar Year			Fiscal Year Ending September 30				5 Month Period Ending February 2
	1944	1945	1946	1947	1948	1949	1950	1951
Income								
Distributive share of income of T. H. Brodhead Co.	$40,537.19	$66,407.96	$57,847.70	$379.23				
Distributive share of income of Ace Distributors					$(3,814.88)	$14,054.66	$(67.08)	$1,882.60
Payments made								
April 19, 1944	1,500.00							
June 9, 1944	420.37							
February 9, 1945	5,265.49							
February 15, 1945	1,500.00							
June 8, 1945	5,954.57							
June 11, 1945	5,000.00							
September 10, 1945	5,265.49							
November 26, 1945	5,000.00							
December 17, 1945	5,265.45							
February 20, 1946	1,253.47							
March 5, 1946	4,112.35	7,677.85						
June 13, 1946		10,210.76						
September 10, 1946		10,210.76						
December 7, 1946		10,210.73						
March 8, 1947		7,468.07						
June 9, 1947		7,118.11						
September 15, 1947		7,093.11						
December 13, 1947		6,418.57	674.54					
February 28, 1948			1,299.98					
February 28, 1948 (loss for fiscal year ending February 28, 1948)			3,814.88		(3,814.88)			
September 23, 1948			315.50					
February 28, 1949			1,315.00					
July 25, 1949			17,500.00					
September 9, 1949			2,500.00					
September 13, 1949			410.75					
February 28, 1950			361.81					
February 28, 1950 (loss for fiscal year ending February 28, 1950)			67.08				(67.08)	
February 28, 1950 (withdrawal of assets for investment in T. H. Brodhead Co., Ltd., at February 28, 1948)			29,588.16	379.23		10,032.61		
September 6, 1950						4,022.05		
	$40,537.19	$66,407.96	$67,847.70	$379.23	$(3,814.88)	$14,054.66	$(67.08)	
Balance								$1,882.60

Exhibit L

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ELIZABETH S. BRODHEAD TRUST

Inventory of Assets
February 28, 1951

Cash				$ 3,858.
Partnership Equity in Ace Distributors				2,904.
Accounts Receivable				
Received as partial liquidation of Ace Distributors				17,000.
Stocks				
4,000	Shares	T. H. Brodhead Co., Ltd.	$40,000.00	
100	"	Hawaiian Electric "E", 5% Pfd.	1,934.50	
50	"	Continental Insurance Co.	3,946.55	
30	"	Insurance Company of North America	4,050.63	
40	"	Texas Company	3,477.60	53,409.
First Federal Savings and Loan Association of Hawaii				8,500.
				$85,673.

Exhibit 22

Schedule of Federal Fiduciary Tax Return Filed

	Fiscal Year Ending September 30,							
	1943	1944	1945	1946	1947	1948	1949	1950
Income								
Partnership and other fiduciaries	$34,319.30							
Interest		$2,000.00	$2,250.00	$2,003.47	$1,787.36	$1,450.00	$1,861.70	$ 704.90
Dividends			892.50	1,264.11	1,952.94	2,128.94	2,543.19	2,880.46
Gain or (loss) on sale of capital assets						(7.53)		
Total income	$34,319.30	$2,000.00	$3,142.50	$3,267.58	$3,740.30	$3,571.41	$4,404.89	$3,585.36
Deductions								
Trustee fees	$ 366.81	$ 185.00	$ 175.19	$ 316.26	$ 297.35	$ 305.10	$ 342.18	$ 280.70
Contributions	10.14							
Bank charges		.05	.20	.15	.05			.05
Taxes			29.65	43.34	33.45	61.12	52.50	77.01
Tax service fee							25.00	35.00
Postage								.26
Total deductions	$ 376.95	$ 185.05	$ 205.04	$ 359.75	$ 330.85	$ 366.22	$ 419.68	$ 393.02
Balance	$33,942.45	$1,814.95	$2,937.46	$2,907.83	$3,409.45	$3,205.19	$3,985.21	$3,192.34
Amount distributed*	33,942.45							
Net income taxable to fiduciary	None	$1,814.95	$2,937.46	$2,907.83	$3,409.45	$3,205.19	$3,985.21	$3,192.34
Tax paid	None	$ 394.44	$ 669.36	$ 577.35	$ 653.68	$ 553.66	$ 696.98	$ 543.48

* Represents amount not actually distributed, but included as income of petitioner, Thomas H. Broomhead, prior to passage of Revenue Act of 1943.

Exhibit 23

ELIZABETH S. BRODHEAD TRUST

Schedule of Federal Fiduciary Tax Returns Filed

	Calendar Year				Fiscal Year Ending September 30, (Note)			
	1943	1944	1945	1946	1947	1948	1949	1950
Income								
Partnerships and other fiduciaries		$40,895.44	$67,914.53	$59,963.42	$ 976.73	$(5,487.84)	$(7,978.48)	$(328.65)
Gain from sale or exchange of capital assets							10,088.95	131.25
Total income	None	$40,895.44	$67,914.53	$59,963.42	$ 976.73	$(5,487.84)	$ 2,110.47	$(197.40)
Deductions								
Interest		$ 1,500.00	$ 1,500.00	$ 1,253.47	$1,000.00	$ 1,000.00	$ 1,410.75	
Trustee commissions		420.37	689.08	603.48		615.00	300.00	$ 300.00
Contributions		302.72	2,394.48	1,839.61	58.50	18.50		
Taxes				2,105.92	350.92		5.75	
Tax service fee					25.00		15.00	15.00
Notary fees						.50		.50
Total deductions	None	$ 2,223.09	$ 4,583.56	$ 5,802.48	$1,434.42	$ 1,634.00	$ 1,731.50	$ 315.50
Net income taxable to fiduciary	None	$38,672.35	$63,330.97	$54,160.94	$ (457.69)	$(7,121.84)	$ 378.97	$(512.90)
Tax paid	None	$19,912.09	$28,737.09	$28,372.42	None	None	$ 46.31	None

Note: Permission to change basis of filing Federal Income Tax Returns from calendar to fiscal year granted per letter of September 1, 1947 from Commissioner of Internal Revenue.

Exhibit 24

[Title of Tax Court and Cause No. 29392.]

REPLY

Come now, Thomas H. Brodhead and Elizabeth S. Brodhead, petitioners, above named, by their attorneys, Milton Cades and Urban E. Wild, and for answer to the allegations of facts contained in respondent's Amendment to Answer heretofore filed herein, admit, deny and allege as follows:

VI.

(1) Admit the allegations contained in paragraph VI (1) of the Amendment to Answer;

(2) Admit the allegations contained in paragraph VI (2) of the Amendment to Answer;

(3) Deny the allegations contained in paragraph VI (3) of the Amendment to Answer;

(4) Admit the allegations contained in paragraph VI (4) of the Amendment to Answer.

/s/ MILTON CADES,
/s/ URBAN E. WILD,
Attorneys for Petitioners.

Of Counsel:

SMITH, WILD, BEEBE & CADES.

[Endorsed]: T. C. U. S. Filed June 25, 1951.

[Title of Tax Court and Causes Nos. 29391-2.]

FINDINGS OF FACT AND OPINION

A trust created by the husband-petitioner for minor children, only one of whom was then in being, became a special partner in a partnership in which the petitioner was the general partner. The next year, when the petitioners had two children, the wife-petitioner created a trust for minor children, which trust purchased the interest of the first trust in the partnership and became a special partner. The trusts' contributions to the partnership originated with the husband. The trusts were long-term trusts, irrevocable, and the trustees were independent of the Settlors.

Held, that the trusts were bona fide partners in the partnership and their distributive shares of partnership income were not income of the settlors.

Held, further, that the settlors did not retain sufficient control over, or interest in, the trusts to make the trust income taxable to them.

Milton Cades, Esq., and Urban E. Wild, Esq., for the petitioners.

Charles W. Myquist, Esq., for the respondent.

The respondent determined deficiencies in income tax for the years and in the amounts as follows:

1943—$42,280.89	1945—$ 48,666.11
1944—$79,944.90	1948—$ 1,177.22

The principal cause of the deficiencies is the inclusion in income of the petitioners of income of successive trusts created by the petitioners—the first

by the husband and the second by the wife—each of which trusts became a partner with the husband in a business which the husband had theretofore operated. The propriety of such inclusion is the main issue. If that issue is decided adversely to the petitioners, there is a further issue as to whether the statute of limitations has run against the year 1943.

Findings of Fact

The petitioners at all times material to these proceedings were husband and wife and residents of the Territory of Hawaii. They filed their income tax returns with the Collector of Internal Revenue for the District of Hawaii.

The petitioners have three children born December 29, 1939, November 19, 1942, and May 1, 1945.

In and prior to 1942 the petitioner Thomas H. Brodhead was engaged as an individual in operating a wholesale merchandise business in Honolulu. The merchandise handled consisted of a great variety of articles which were sold to post exchanges and ships' service stores and included drug items, razor blades, dungarees, shoes, underwear, work shirts, shower clogs, pocket knives, candy, gum, and miscellaneous items.

The petitioner Thomas H. Brodhead came from a family of short-lived people on his father's side and he was quite concerned about the length of his own life. Conditions in Hawaii in 1942 were not conducive to a feeling of long life. He was determined to make some provision for his children so that they would have a better education than he

had. In September, 1942, the petitioners had one child, and were expecting the birth of another. Thomas H. Brodhead's business grew rapidly after the start of World War II, and he wanted some means of having it carried on for the benefit of his children in the event of his death. Also, because of the size to which the business had grown in 1942 he felt that he needed someone to help him with it.

Mortimer J. Glueck had been a personal and business acquaintance of the petitioner Thomas H. Brodhead for a number of years, had kept his books on a part-time basis, and had advised him generally. Glueck had a commission business, and in 1942 he was getting too busy with it to be able to assist petitioner Brodhead and advised him to get other assistance. Glueck and Brodhead had many discussions as to what provision the latter should make for his children.

Bishop Trust Company, Limited, in and prior to 1942 conducted a trust company business in the Territory of Hawaii. It is operated as a professional fiduciary, with side issues such as insurance, real estate sales, and brokerage. Its main business is the administration of estates, trusts, guardianships and agency accounts. The normal trust or estate handled by the trust company consists of securities or interests in real estate. However, it has at times administered proprietorships and the controlling shares of incorporated businesses. In the administration of such properties it has operated various businesses including a structural steel mill, a department store, dairies, ranches, a bottling company, and an automobile agency.

In 1942 Glueck and Brodhead sought the advice of counsel, and it was agreed that a trust should be created for the benefit of the petitioners' children and that the trust should become a partner with Brodhead in his business. Brodhead asked Glueck to be one of the trustees so that with his knowledge of the business he could carry it on in the event of Brodhead's death. Brodhead also wanted Bishop Trust Company, Limited, as a trustee for the general assistance and advice that it could give.

On September 30, 1942, the petitioner Thomas H. Brodhead created the Thomas H. Brodhead Trust, naming Mortimer J. Glueck and Bishop Trust Company, Limited, as trustees. Corpus of the trust was stated to be $40,000. It consisted of a one-half interest in the petitioner's business which at that time had a net worth of $80,000. Under the trust agreement, the $40,000 corpus was to be contributed to the capital of a special partnership to be organized concurrently for a 50 per cent interest therein.

The trustees were required to accumulate all trust income during the continuance of the trust, but they had discretion to pay out net income for the maintenance, support and education of the children of the settlor, or if income was insufficient they could use corpus. All income not used for such purposes was to be accumulated and added to corpus. The trustees were authorized to pay to any child of the settlor any time after attaining age 21, as they deemed proper, such portion of corpus and ac-

cumulated income as constituted one share, such share to be determined by considering the trust estate to be divided into as many equal shares as there should be children then surviving or lineal descendants of any deceased child.

The trust was to continue until 20 years after the death of the settlor. The trust property and accumulated income were then to be distributed to the surviving children of the settlor (other than those to whom the distribution of a share may have previously been made) and the issue of any deceased children. If there were no children or issue then surviving, distribution was to be made to those persons, other than the settlor, who would be the heirs-at-law of the last survivor of the children of the settlor.

The trustees could terminate the trust at any time after the termination of the special partnership, in which event distribution was to be made to the settlor's children and issue of any deceased children.

The trustees were given broad powers to invest and reinvest and manage the trust property, but during the life of the settlor they were required to obtain his consent to all investments. After the settlor's death the trustees were to be restricted in making investments to those which trustees are permitted by law to make. However, they could in any event make advances or loans to the special partnership without liability for any loss resulting therefrom.

The settlor reserved the right to transfer addi-

tional property to the trust. The trustees were required to furnish annual statements of account to the beneficiaries. The corporate trustee was given the custody of all money or securities in the trust.

The trust was declared to be irrevocable by the settlor. It was provided that in no event should any of the trust property or income be paid to or inure to the benefit of the settlor.

Any alteration, amendment, cancellation or revocation of any provisions of the trust required the written consent of the trustees and all of the beneficiaries.

A special partnership was formed by a document dated as of September 30, 1942. The petitioner Thomas H. Brodhead was referred to therein and signed the agreement as "General Partner". The trustees of the above described trust are referred to and signed as "Special Partner." The partnership adopted the name of T. H. Brodhead Co. Its purpose was to acquire the assets and carry on the business theretofore conducted by the petitioner Thomas H. Brodhead. Other purposes are stated including the carrying on of any business that may lawfully be carried on by a partnership.

The initial capital of the partnership was $80,000 which was the book value of the net assets that it acquired. It was agreed that $40,000 was the capital contribution of each of the partners and that each had a 50 per cent interest.

The general partner who was actively engaged in the business was to receive compensation for his services which was to be charged as an expense in

computing partnership profits. The remaining profit or loss, was to be divided in proportion to the capital contributions. Profits attributable to each partner's interest could be withdrawn from time to time as the partners deemed advisable.

The trustees had all the powers, rights and duties of a special partner as prescribed by designated sections of the Special Partnership Law of the Territory of Hawaii, and were not liable for partnership debts beyond the extent prescribed by law.

Only the general partner had authority to transact the business of the partnership, or incur obligations. He was to establish the policy of the partnership. The special partner could at all times investigate the partnership affairs and advise the general partner as to its management.

The general partner could not assign or mortgage any part of his interest. The special partner could assign its interest with the consent of the general partner.

Proper partnership books and records were to be kept and each partner was to have full access to them. The books were to be audited at least once a year, and a copy of the auditor's report was to be delivered to each partner. Annual accounts were to be taken, showing the capital of the partnership and the interest of each partner therein and copies were to be furnished each partner.

The partnership could be terminated by the general partner on two months' written notice. On termination, debts were to be paid, and any balance remaining was to be applied first to advance ac-

counts of the partners, then to capital, then between the partners in the manner provided for division of profits. If the balance after payment of debts was insufficient to pay in full the advance accounts of all partners, the special partner was to be paid first.

In the event of the death of the general partner, his representative had the option of succeeding to or carrying on his interest in the business as a general partner.

The partnership was to continue for a ten-year period and thereafter from year to year until terminated by either partner giving three months' notice.

By bill of sale dated as of the close of business on September 30, 1942, the petitioner Thomas H. Brodhead conveyed to the special partnership the rights, property, assets and privileges owned by him and used in his merchandising business. The partnership agreed in the bill of sale to assume the liabilities disclosed by the balance sheet attached thereto. The balance sheet listed assets in the amount of $178,598.73, current liabilities in the amount of $98,598.73, and capital in the amount of $80,000. Among the assets listed were cash, $21,532.34; accounts receivable, $64,667.35; and merchandise inventory, $27,310.44.

The required documents concerning the organization of the special partnership were duly filed and publication was made in a Honolulu paper.

Early in 1943, the petitioner Thomas H. Brodhead was advised by his attorney that under a re-

cent court decision he might be subject to Federal income tax on all of the income of the Thomas H. Brodhead trust without being able to get any of the trust income to use to pay the tax. In that situation, it was possible that he might have been unable to pay the tax. He was advised by counsel that a new trust could be created, omitting the features that might make the income of the first trust taxable to him, to acquire the interest of the first trust in the partnership.

Following discussions among the petitioners, the trustees of the Thomas H. Brodhead trust, and counsel, the petitioner Elizabeth S. Brodhead on February 28, 1943, created the Elizabeth S. Brodhead trust. The trustees of that trust were the same as those of Thomas H. Brodhead trust. At that time, Thomas H. Brodhead gave his wife $10,000 which she paid in to the trust created by her. Both petitioners filed federal gift tax returns in which they reported the gifts of $10,000 made by them.

The provisions of the Elizabeth S. Brodhead trust were substantially the same as those of the Thomas H. Brodhead trust. The principal differences were that the wife's trust did not give discretion to the trustees to distribute income for maintenance, support or education of the beneficiaries during minority, and it was to terminate when the youngest child attained the age of 33 years.

On February 28, 1943, the Elizabeth S. Brodhead trust purchased from the Thomas H. Brodhead trust its 50 per cent interest in the special partnership. That interest was duly assigned to the Eliza-

beth S. Brodhead trust by an instrument dated February 28, 1943, in which Thomas H. Brodhead, as general partner, gave his consent to the assignment. The Elizabeth S. Brodhead trust paid the Thomas H. Brodhead trust the sum of $10,000, and gave its note for the unpaid balance of the purchase price of the 50 per cent interest in the amount of $30,000 with interest at 5 per cent. Interest was paid periodically, and the principal of the note was paid off by payments made in 1945 and 1949. The legally required certificate of change of the special partnership and affidavits were duly filed, and notice was duly published.

An independent firm of auditors was employed by the partnership to make audits of the partnership business and to prepare annual statements.

The petitioner Thomas H. Brodhead received compensation for his services to the partnership for the periods and in the amounts as follows:

Period or Year	Amount
Oct. 1, 1942, to Feb. 28, 1943	$ 6,250.00
Fiscal year ended Feb. 28, 1944	15,000.00
Fiscal year ended Feb. 28, 1945	18,000.00
Fiscal year ended Feb. 28, 1946	18,000.00
Fiscal year ended Feb. 28, 1947	18,000.00

As of the close of business on February 28, 1947, the name of the special partnership was changed from T. H. Brodhead Co. to Ace Distributors. The instrument changing the name was executed by Thomas H. Brodhead as general partner and by Mortimer J. Glueck and Bishop Trust Company,

Limited, trustees under the Elizabeth S. Brodhead trust as special partner. The necessary documents to effect the change were duly filed and publication was duly made.

As of the close of business on February 28, 1947, the partnership, under its new name of Ace Distributors, assigned to T. H. Brodhead Co., Ltd., an Hawaiian corporation, certain rights, property and assets used in its business, subject to balance sheet liabilities, which properties had a net book value of $80,000. In payment therefor the corporation issued 4,000 shares of its stock to the general partner and an equal number to the special partner. The necessary documents in connection with the organization of the corporation and the issuance of its stock were duly filed.

During the period of operations of the special partnership, the general partner discussed the problems of the business frequently with the trustees of the two trusts. Whenever a financial report on the business was issued he furnished copies to the trustees. The general partner conferred with the corporate trustee as to investment of the funds of the first trust. In one instance it accepted his suggestion as to an investment and in another instance it refused to do so. He discussed with the trustees possible means of financing an expansion of the partnership business which in the war years was increasing in volume.

The partnership T. H. Brodhead Co. filed partnership returns on an accrual and fiscal year basis ending on the 28th of February. Its first return on

that basis was filed for the fiscal year ended February 28, 1943. Returns were filed on that basis for each of the subsequent fiscal years 1944 through 1949.

The Thomas H. Brodhead trust and the Elizabeth S. Brodhead trust filed Federal fiduciary returns each year and duly paid the tax shown to be due thereon. None of the funds of the trusts has ever been paid out to the beneficiaries thereof. Out of the income of the trusts there have been paid the expenses of each, such as trustee fees, tax service fees, and the Federal and territorial income taxes.

On September 30, 1950, the assets of the Thomas H. Brodhead trust amounted to a total of $86,918.97 which consisted of cash in the amount of $2,109.48 and investments in stocks, bonds, and savings and loan certificates with a cost of $84,809.49.

On February 28, 1951, the assets of the Elizabeth S. Brodhead trust amounted to a total of $85,673.03, which was made up of cash, $3,858.90; partnership equity in Ace Distributors, $2,904.85; accounts receivable received in partial liquidation of Ace Distributors, $17,000; 4,000 shares of stock in T. H. Brodhead Co., Ltd., $40,000; other stocks having a cost of $13,409.28; savings and loan certificates with a cost of $8,500.

The joint Federal income tax return of the petitioners for the year 1943 was filed with the Collector on or about March 20, 1944. The gross income shown thereon was in the amount of $74,888.57. On or about January 18, 1949, the petitioners and

the respondent executed a consent extending to June 30, 1950, the period within which an income tax may be assessed or a deficiency notice mailed to the petitioner for the year 1943.

The deficiency notices in these proceedings were mailed to the petitioners on February 7, 1950.

The petitioner Thomas H. Brodhead and the trustees of the Thomas H. Brodhead trust and of the Elizabeth S. Brodhead trust really and truly intended to, and did, join together for the purpose of carrying on the business of T. H. Brodhead Co. and sharing in its profits and losses.

The two trusts were bona fide trusts for the benefit of the children of the settlors, and the petitioners had no substantial control over, or interest in, the corpus or income thereof.

Opinion

Arundell, Judge: The respondent has determined, as set forth in the notices of deficiency, that "the T. H. Brodhead Company, (Ace Distributors in 1948) an alleged partnership * * * is not a valid partnership for Federal income tax purposes" with the consequence that all of the income from such partnership is taxable to the petitioners. This determination is assigned as error.

An alleged error concerning a deduction for legal fees for the year 1943 has been abandoned by the petitioners.

While the pleadings are directed to the question

of the validity of the special partnership, the parties argue not only that question but also that of whether the income reported by the trusts is taxable to the petitioners under the rationale of Helvering v. Clifford, 309 U.S. 331.

The partnership question. It is our opinion, and we so hold, that the successive trusts were bona fide partners in the partnership of T. H. Brodhead Co. (the name of which was changed in 1947 to Ace Distributors).

The ultimate factual question in the tax treatment of family arrangements in the form of partnerships is "whether, considering all the facts * * * the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise." Commissioner v. Culbertson, 337 U.S. 733. The evidence satisfies us that in forming the partnership the parties were acting in good faith and with a business purpose. There is no doubt that Thomas H. Brodhead was genuinely concerned about the possibility of his death, which event would have affected his one-man business. The welfare of his family was tied in with the degree of success of the business. In order to insure, as far as possible, that neither would suffer in the event of his untimely death, the partnership was formed. There was a business purpose in bringing in Glueck and the trust company as a special partner. Glueck had been Brodhead's business advisor, and an employee in the business. In those capacities he had a good grasp of the various aspects of the

business and was in a position to carry it on if that became necessary. Brodhead wanted the trust company as a participant because of its broad experience in the management of businesses and for the advice that it could give in the operation of a rapidly expanding business. While a special partner cannot transact the business of the partnership, it may at all times investigate partnership affairs and advise the partners as to management.[1] The parties did join together in the present conduct of the enterprise theretofore conducted by Brodhead alone. Brodhead irrevocably parted with a 50 per cent interest in the net assets of the business, and with 50 per cent of the profits of the business after compensation for his services.

Capital was a material income-producing factor in the business of the partnership. The contribution made by each of the trusts was capital—as distinguished from services. The fact that it was gift capital which originated with the petitioners does not preclude recognition of it as a genuine capital contribution where the facts indicate "that the amount thus contributed and the income therefrom should be considered the property of the donee for tax, as well as general law, purposes. * * * Whether he [the donee] is free to, and does, enjoy the fruits of the partnership is strongly indicative of the

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[1] Revised Laws of Hawaii, 1935, as amended, ch. 225, section 6881.

reality of his participation in the enterprise." Commissioner v. Culbertson, supra; Theodore D. Stern, 15 T.C. 521.

The respondent contends against the recognition of the trusts as partners because of the settlors' control over corpus and income. Corpus was required to be paid into the business of which Brodhead was the manager. Distributable income was what was left after Brodhead took out his salary. We do not see wherein these factors should serve to operate against recognition of the trusts as partners, at least in the absence of any abuse by Brodhead of his discretion in his handling of corpus or income. Trusts normally provide for some degree of control over corpus and/or income by someone other than the beneficiary. If they did not, the transfer would result in an outright gift rather than the creation of a trust.[2] The question of the tax effect of retained control is one of degree, as is true of many questions in the law. " 'Drawing the line' is a recurrent difficulty in those fields of the law where differences in degree produce ultimate differences in kind". Harrison vs. Schaffner, 312 U. S. 579. The question of where to draw the line as to the permissible degree of control which will shift tax liability is of particular concern where income is produced by property rather than by services. In such cases, the tax liability attaches to

[2] In the case of an inter vivos trust where the settlor retains power to control the trustee in some respects in the administration of the trust, the settlor is ordinarily under a fiduciary duty to the beneficiary in respect to the exercise of the power. Scott, The Law of Trusts, section 185.

ownership. Poe vs. Seaborn, 282 U. S. 101, Hoeper vs. Tax Commission, 284 U. S. 206. A beneficiary of a trust may assign a share of the trust income to another for life without retention of any form of control, and such assignment is treated as a transfer in praesenti of a life interest in the trust corpus with income taxable to the donee. Blair vs. Commissioner, 300 U. S. 5. One step removed from such complete assignment is the assignment of trust income for a limited period. In such a case, the gift of the income "for the period of a day, a month or a year involves no such substantial disposition of the trust property as to camouflage the reality" that the assignor continues to enjoy the benefit of the trust income. Harrison vs. Schaffner, supra. Still further removed are situations like those involved in Helvering vs. Clifford, supra, where the owner of property places it in trust for a relatively short term, with himself as trustee, retains broad powers of management and over distribution of income, with a reversion to the grantor. A gift in trust for the benefit of another, but with reserved power to modify or revoke, results in taxation of the trust income to the settlor. This is on the ground that "taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed—the actual benefit for which the tax is paid". Corliss vs. Bowers, 281 U. S. 376.

The attribution of income from property to the owner of the property was emphasized by the Tax Committees of the House of Representatives and of the Senate in their consideration of the family

partnership provisions that became section 340 of the Revenue Act of 1951[3]. It was the expressed view of the committees that partnership income, where capital is a material income-producing factor, should be taxed to the partners if they were the real owners of their interests regardless of how the interests may have been acquired.

While purported intra-family gifts may be mere shams, not every restriction upon unfettered control is to be regarded as indicative of sham in the transaction. Lack of true ownership in the transferee is not necessarily indicated by powers retained by the transferor as a managing partner or in any other fiduciary capacity when considered in the light of all of the circumstances.[4]

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[3] H. Rep. No. 586, 82nd Cong., 1st sess.; 1951 I.R.B. No. 23, p. 31, at p. 54. The Senate Finance Committee issued a report in the same language as the Ways and Means Committee Report. See S. Rep. No. 781, 82nd Cong., 1st sess.; 1951 I.R.B. No. 24, p. 40, at p. 67.

[4] "Not every restriction upon the complete and unfettered control by the donee of the property donated will be indicative of sham in the transaction. Contractual restrictions may be of the character incident to the normal relationships among partners. Substantial powers may be retained by the transferor as a managing partner or in any other fiduciary capacity which, when considered in the light of all the circumstances, will not indicate any lack of true ownership in the transferee. In weighing the effect of a retention of any power upon the bona fides of a purported gift or sale, a power exercisable for the benefit of others must be distinguished from a power vested in the transferor for his own benefit." (H. Rep. No. 586, supra.)

The family partnership provisions enacted as section 340 of the Revenue Act of 1951 are not retroactive to the years involved in these proceedings. Nevertheless, the basic principle of taxing income from property to the owner of the property was the law in the earlier years as fully as it is today. A proper appraisal of the evidence is convincing that the trusts in these proceedings were the owners of the property held by them. Petitioner T. H. Brodhead irrevocably parted with a 50 per cent interest in his business property when he created the first trust. The second trust became the owner of that interest by purchase. The corpus has not reverted to him, and it cannot. The income has not been used for the benefit of the settlers but is held intact for the beneficiaries. Such powers as Brodhead had over the corpus by use in his business were no more than those of a managing partner, and in the exercise thereof he was required to act in a fiduciary capacity. After a gift is once complete and title has passed to the donee, the fact that the donor subsequently has possession of it does not affect its validity. Garrison vs. Union Trust Co., 164 Mich. 345, 129 N.W. 691; Adams vs. Hagerott, 34 F. 2d 899.

This is not a case like Ralph C. Hitchcock, 12 T.C. 22, where a father purported to make gifts to minor children of interests in his business, had himself appointed guardian, and charged their purported distributive shares with the cost of their board and keep. Here we have independent trustees

who received the full distributive share of the trusts for the benefit of the children.

We fail to see wherein the restrictions on the limited partner were such as to invalidate the partnership. The prohibition against transaction of partnership business by the special partner is a normal provision of limited partnership agreements, and in fact is usually provided for by law where limited partnerships are recognized. See Theodore D. Stern, supra, where we said that retained control in the general partner "is of no particular significance since limited partners normally have no part in the control or management of the business." 15 T.C. at p. 527.

No question is raised in these proceedings as to whether under the laws of Hawaii a trust may be a member of a special partnership. Neither the statutes of Hawaii nor Internal Revenue Code section 2797 prohibit a trust from being a partner, and we have recognized that trusts can be members of partnerships. See Louis R. Eisenmann, et al., 17 T.C. (Feb. 29, 1952), and Theodore D. Stern, supra. See also Greenberger vs. Commissioner, 177 F. 2d 990.

The Clifford case question. We hold that the decision in the case of Helvering vs. Clifford, supra, is not controlling in these cases. The factual differences are so great as to obviate any need for extended discussion. Here we have long-term trusts—the first was to continue until 20 years after the death of the settlor, and the second until the youngest beneficiary attained the age of 33

years. The settlors in these proceedings were not the trustees. They had no discretion as to distribution of income. There could be no reversion of corpus to the settlors.

The respondent makes an argument that the petitioner Thomas H. Brodhead could control the amount of income of the trusts through siphoning off partnership income as compensation for his services. There is no indication that the compensation of Brodhead was more than a reasonable sum for services rendered. Moreover, any compensation taken by him in excess of a reasonable amount would be inconsistent with the purpose for which the respondent charges the trusts and partnership were created, namely, to avoid taxation of income of the business to Brodhead. Also, we have here independent trustees who had available and who, it must be assumed, would use means of preventing the general partner from depriving the trustees' wards of their rightful share of partnership income. A partner does not stand only as such in partnership matters; he occupies a fiduciary relationship to the other partners in all partnership matters and the utmost good faith is required of each in their relations to each other. 68 C.J.S., Partnership, section 76; Stem vs. Warren, et al., 161 N.Y.S. 247. Here the outcome of the partnership operations, mentioned above, indicates as a practical matter entire good faith on the part of the general partner in his dealings with the special partner which inured to the benefit of the trust beneficiaries.

By amended answer, the respondent invokes the

provisions of section 275(c) of the Internal Revenue Code to avoid the operation of the statute of limitations against assessment for the year 1943. This question would require decision only in the event that the trust-partnership income was properly taxable to the petitioners, and if that income was in excess of 25 per cent of reported gross income. As we have held that such income was not income of the petitioners, we do not decide the limitations issue.

Decisions will be entered under Rule 50.

The Tax Court of the United States
Washington

Docket No. 29391

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DECISION

Pursuant to the Opinion of the Court promulgated July 7, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioners herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there is a deficiency in income tax for the taxable year 1948 in the amount of $18.98.

Entered October 31, 1952.

[Seal] /s/ C. R. ARUNDELL,
Judge.

The Tax Court of the United States
Washington

Docket No. 29392

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Petitioners.

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DECISION

Pursuant to the Opinion of the Court promulgated July 7, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioners herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there is an overpayment in income and victory tax for the taxable year 1943 in the amount of $42,498.49 of which $62.96 is barred from refund by statute and the balance of which, in the amount of $42,435.53, was paid within two years before the execution of an agreement to extend the time prescribed by section 275 of the Internal Revenue Code for assessment;

that there is an overpayment in income tax for the taxable year 1944 in the amount of $43,087.69, all of which was paid two years before the execution of an agreement to extend the time prescribed by section 275 of the Internal Revenue Code for assessment; and that there is a deficiency in income tax for the taxable year 1945 in the amount of $2,496.65.

Entered October 31, 1952.

[Seal] /s/ C. R. ARUNDELL,
Judge.

In the United States Court of Appeals
for the Ninth Circuit

T.C. Docket Nos. 29391-29392

COMMISSIONER OF INTERNAL REVENUE,
Petitioner on Review,
vs.
THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Respondents on Review.

PETITION FOR REVIEW

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decisions entered by The Tax Court of the United States in these proceedings on October 31, 1952, "That there is a deficiency in income tax for the taxable year 1948 in the amount of $18.98" and "That there is an overpayment in income and victory tax for the

taxable year 1943 in the amount of $42,498.49 of which $62.96 is barred from refund by statute and the balance of which, in the amount of $42,435.53, was paid within two years before the execution of an agreement to extend the time prescribed by section 275 of the Internal Revenue Code for assessment; that there is an overpayment in income tax for the taxable year 1944 in the amount of $43,-087.69, all of which was paid two years before the execution of an agreement to extend the time prescribed by section 275 of the Internal Revenue Code for assessment; and that there is a deficiency in income tax for the taxable year 1945 in the amount of $2,496.65." This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The respondents on review, Thomas H. Brodhead and Elizabeth S. Brodhead, are husband and wife whose mailing address is 843 Kaahumanu Street, Honolulu, Territory of Hawaii, and who resided during the taxable years in Hawaii. The taxpayers filed their Federal income tax returns for the calendar years 1943, 1944, 1945 and 1948, the taxable years here involved, with the Collector of Internal Revenue for the District of Hawaii.

Nature of Controversy

The sole question which was presented to and passed upon by The Tax Court of the United States is whether the income of a partnership in which the taxpayer, Thomas H. Brodhead, was a general partner, and a trust created for the benefit of the

taxpayers' minor children was designated as a special partner, was taxable to the taxpayers, in so for as the share thereof allocable to the trust was concerned, under the doctrine of Helvering vs. Clifford, (1940) 309 U.S. 331, as well as the income of an earlier trust created by the husband for the benefit of their children which earlier trust was superseded as a special partner in 1943 by a trust created in 1943.

In and prior to 1942, the taxpayer, Thomas H. Brodhead, was engaged as an individual in operating a wholesale merchandise business in Honolulu, the merchandise handled by his business consisting of a great variety of articles which were sold to post exchanges, and ships' service stores. On September 30, 1942, the taxpayer, Thomas H. Brodhead, created, for the benefit of his children, the Thomas H. Brodhead Trust, the Bishop Trust Company, Limited, and Mortimer J. Glueck being named as trustees. The corpus of the trust consisted of a one-half interest in the taxpayer's business, stated to be the sum of $40,000, which corpus, under the trust agreement, was to be contributed to the capital of a special partnership to be organized for a 50 per cent interest in such partnership. On the same date, September 30, 1942, a special partnership was formed, called the T. H. Brodhead Company, of which partnership Thomas H. Brodhead was designated as "General Partner" and the trustees of the trust hereinabove mentioned were referred to as "Special Partner." It was agreed that $40,000 was the capital contribution of each

of the partners and that each had a 50 per cent interest in the partnership. Only the general partner had authority to transact the business of the partnership, or to incur obligations. The taxpayer, Thomas H. Brodhead, conveyed to the special partnership the rights, property, assets, and privileges owned by him and used in his merchandising business and the partnership agreed in the bill of sale to assume the liabilities disclosed by the balance sheet of the business attached thereto.

On February 28, 1943, the taxpayer's wife, Elizabeth S. Brodhead, created the Elizabeth S. Brodhead Trust, for the benefit of their children, the trustees of which latter trust were the same as those of the Thomas H. Brodhead Trust. Thomas H. Brodhead gave his wife $10,000 which she paid in to the trust created by her. On the same date, February 23, 1943, the Elizabeth S. Brodhead Trust purchased from the Thomas H. Brodhead Trust its 50 per cent interest in the special partnership, having paid to Thomas H. Brodhead Trust the sum of $10,000 and having given its note for the unpaid balance of the purchase price of the 50 per cent interest in the amount of $30,000 with interest at 5 per cent. Thereupon the Elizabeth S. Brodhead Trust became a special partner. The name of the partnership was changed from T. H. Brodhead Company to Ace Distributors on February 28, 1947.

In his notices of deficiencies, the Commissioner held that the partnership was not a valid partnership and that all of the income of the alleged partnership (computed on the basis of fiscal years

ending on the 28th of February) a portion of which had been reported in fiduciary returns filed by the Thomas H. Brodhead Trust and the Elizabeth S. Brodhead Trust, was taxable to the taxpayers, Thomas H. Brodhead and his wife, Elizabeth S. Brodhead. In making his determinations the Commissioner allocated the fiscal year incomes of the partnership to the taxpayers on a calendar year basis. The Tax Court of the United States disagreed with the Commissioner's determination and held that the trusts were bona fide partners in the partnership and that their distributive shares of partnership income were not income of the taxpayer settlors. The Court held, further, that the settlors did not retain sufficient control over, or interest in, the trusts to make the trust income taxable to them.

/s/ CHARLES S. LYON,
Assistant Attorney General
/s/ CHARLES W. DAVIS,
Chief Counsel Bureau of Internal Revenue
Attorneys for Petitioner on Review

[Endorsed]: T.C.U.S. Filed Jan. 19, 1953.

[Title of U. S. Court of Appeals and Causes.]

STATEMENT OF POINTS

Comes Now the Commissioner of Internal Revenue, petitioner on review in the above-entitled causes, by his attorneys, H. Brian Holland, Assist-

ant Attorney General, and Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and hereby states that he intends to rely upon the following points in these proceedings:

The Tax Court of the United States erred:

1. In entering its decisions "That there is a deficiency in income tax for the taxable year 1948 in the amount of $18.98" and "That there is an overpayment in income tax for the taxable year 1943 in the amount of $42,498.49 * * *; that there is an overpayment in income tax for the taxable year 1944 in the amount of $43,087.69 * * *; and that there is a deficiency in income tax for the taxable year 1945 in the amount of $2,496.65."

2. In failing and refusing to sustain the deficiencies in tax determined by the Commissioner.

3. In holding and deciding that the trusts created by the taxpayers for the benefit of their minor children were bona fide partners in the partnership involved and that their distributive shares of partnership profits were not income of the taxpayers herein.

4. In failing and refusing to hold and decide that the trusts created by the taxpayers for the benefit of their minor children were not, for Federal income tax purposes, recognizable partners in the taxpayer's business known as T. H. Brodhead Company, later called Ace Distributors.

5. In holding and deciding that the settlor-taxpayers did not have any rights in the trust corpora or income sufficient to make the income of the trusts taxable to them.

6. In failing and refusing to hold and decide that, under the doctrine of Helvering vs. Clifford, 309 U. S. 331, the income of the trusts created by the settlor-taxpayers for the alleged benefit of their minor children was taxable to the settlor-taxpayers.

7. In that its ultimate conclusion that the trusts created for the taxpayers' minor children were bona fide trusts created for the benefit of the said children and that the taxpayers did not have any substantial control over, or interest in, the corpora or the income of the trusts is not supported by but is contrary to its underlying findings of fact.

8. In that its opinion and its decisions are not supported by but are contrary to the Court's findings of fact.

9. In that its opinion and its decisions are not supported by but are contrary to the evidence.

10. In that its opinion and its decisions are contrary to law and the Commissioner's regulations.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General

/s/ CHARLES W. DAVIS,
Chief Counsel Bureau of
Internal Revenue
Attorneys for Petitioner on Review

Acknowledgment of Service attached.

[Endorsed]: T.C.U.S. Filed April 2, 1953.

[Title of Tax Court and Causes No. 29391-2.]

CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States, do hereby certify that the foregoing documents 1 to 41, inclusive, constitute and are all of the original papers and proceedings, including Exhibits (1 thru 45), attached to the Stipulation of Facts, Respondent's Exhibits (A thru E), admitted in Evidence, on file in my office as the original and complete record in the proceedings before The Tax Court of the United States in the above-entitled proceedings and in which the respondent in The Tax Court proceedings has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceedings, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia this 8th day of April, 1953.

[Seal] /s/ VICTOR S. MERSCH,
Clerk, The Tax Court of the
United States

Before The Tax Court of the United States

Docket No. 29391

In the Matter of: THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

Docket No. 29392

In the Matter of: THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

TRANSCRIPT OF PROCEEDINGS

No. 2 Courtroom, Federal Building, Honolulu, T.H. 9:30 a.m. to 12:40 p.m.—June 20, 1951

Pursuant to notice, the above entitled matter came on to be heard.

Before Honorable C. R. Arundell, Judge.

Appearances:

Urban E. Wild, Esq., Milton Cades, Esq., (Smith, Wild, Beebe & Cades), Bishop Trust Bldg., Honolulu, T.H., appearing on behalf of Petitioners.

Charles W. Nyquist, Esq., (Treasury Department Counsel) appearing on behalf of Respondent. [1*]

THOMAS H. BRODHEAD

Petitioner, called as a witness in his own behalf, being first duly sworn was examined and testified as follows:

The Clerk: Please state your name and address for the record.

The Witness: Thomas Holmes Brodhead, 1468 St. Louis Drive, Honolulu.

Direct Examination

Q. (By Mr. Wild): Mr. Brodhead, are you one of the petitioners in Docket number 29391 and also Docket number 29392 now on trial before the Court? A. I am.

Q. And the other petitioner is Elizabeth S. Brodhead, and she is here in court, is she?

A. She is.

Q. Mr. Brodhead, what business were you engaged in in 1940? A. The wholesale business.

Q. And where?

A. 843 Kaahumanu Street.

Q. In what city?

A. Honolulu, Territory of Hawaii.

Q. And had you been conducting that business for a considerable period of time? [22]

A. I had.

Q. What type of business was it, was it a wholesale or retail business, or what was it?

* Page numbering appearing at foot of page of original Reporter's Transcript of Record.

(Testimony of Thomas H. Brodhead.)

A. It was wholesale.

Q. Wholesale of merchandise, was it?

A. Of general merchandise which consisted of a great variety of items such as drug items, which included tooth paste and brushes, razor blades and associated items that were sold to post exchanges and ships service stores; a great deal of items like dungarees, shoes, underwear and work shirts; miscellaneous items like pocket knives and shower clogs and things like that. In other words, it was a very diversified business because of the essential things that army and navy people bought in the exchange stores. It also included candy, gum and things like that.

Q. Did you also sell fruit juices and other products of that type? A. I did.

Q. Now when was it that you first considered the idea of creating a trust for your child or children that you might have?

A. Well, that had been going on for quite some time before it was actually started. Mr. Glueck and I used to have a lot of conferences because of the fact that he was keeping my books, was my advisor and knew my financial status, and [23] he had known me for a number of years and had opened up my original set of books, so he grew up with the company, or with my business rather, and I was discussing with him when I had chances, of what to do. He was urging me to take steps and I was so busy with the company, or I should call it my own business, that I just didn't get around

(Testimony of Thomas H. Brodhead.)

to it for awhile until things got over my head, you might say, and I just had to make a decision.

Q. Well, about when was it that you finally made a decision?

A. Around August or September after the war started. That would make it 1942.

Q. What was done at that time?

A. Mr. Glueck and myself had sort of a hot discussion between us. He reminded me that I had been going to do it for a long time now. I had to take time away from business and do something about it. So we went to counsel and met Mr. Milton Cades and discussed the matter with him. Mr. Glueck went along with me. We went over the pros and cons of my problems and my thoughts on it, and it developed from there.

Q. Well, what did you desire to do with your business at that time?

A. I was particularly interested in getting assistance, because the business had grown by leaps and bounds, especially after the war started, because I was one of the six signers of a contract on December 10, that opened December [24] 10, 1941, and as a result I was able to get additional business because of the needs of the navy especially.

Q. Well now, come back to your business. What did you yourself decide that you wanted to do with the business, continue it as an individual, or do what with it?

A. I couldn't continue it as an individual. I could have, yes, but it was too risky. It was getting

(Testimony of Thomas H. Brodhead.)

up into figures that were scaring me, and I knew that I had everything invested in there, and I didn't want to risk everything. I needed somebody to help me, and I also wanted to look after my children. We had one then. When my wife and I were married I asked her to agree to two or none, because I am an only child. I wanted to see that they were provided for and have the education which I did not have, and that was the main thing.

Q. Well, what did you do as a result of that determination and your conference or conferences?

A. It was decided that we would set up a trust for the children.

Q. Who are the "we" you talk of?

A. Mr. Glueck, Mr. Cades and myself, because it was a three-way discussion, to set up a trust for the children and that I would manage that, but that it the same time would get the assistance of the trust company for advice.

Mr. Wild: I didn't get that last answer. Will [25] you read the answer, please?

(The last answer was read by the reporter.)

Q. (By Mr. Wild): Did you mean by that that you were going to run the trust?

A. Absolutely not.

Q. Well, what were you going to manage? What were you referring to?

A. The business itself.

Q. I see. And what was the trust capital to consist of?

(Testimony of Thomas H. Brodhead.)

A. Everything I had was in the business. That was it.

Q. Well, do you mean to say by that that you were turning your whole business into this trust?

A. No, we would take the value of the business at that time and split it into two parts, one part for the trust company and one part for myself.

Q. And at that time did you also discuss as a part of the proceedings a formation of a special partnership, a partnership to take over the business?

A. You mean a partnership with the trust company and myself?

Q. That's right, a partnership, did you discuss it? A. That is correct.

Q. And what was decided to be done in regard to that?

A. In that case I was to run the business.

Q. No, I am not asking you who was in control of the [26] business. I am just asking you what you decided to do, if anything, about a partnership?

A. Well, it was later decided in consultation with the three of us that the Bishop Trust Company would be the special partner.

Q. And was anyone else to be a special partner with them? A. Yes.

Q. Who was that?

A. I requested that Mr. Glueck be a special partner with them in view of the fact that he had been my accountant for years. He then had his office in my building, the same building that I was

(Testimony of Thomas H. Brodhead.)

in, and he had grown up with the business. I had a lot of confiidence in him, and he was formerly a roommate of mine when we were bachelors at Waikiki Beach.

Q. At that time had he told you anything about whether he could continue to keep your books and act for you as he had before?

A. That was one of the main things that made me do this, was the fact that he said he could not continue on. The business was getting too big, and he didn't feel capable of advising me alone.

Q. Let me ask you this question: Was overseeing your books his only business?

A. No, this was a sideline for him. He was doing it as an accommodation at no salary, and he said that he just [27] couldn't keep it up, which fact I appreciated, but I hated to lose him.

Q. What business was he in?

A. At what time are you referring to?

Q. At this time when you were discussing setting up the special partnership, when you asked that he be a special partner.

A. He was in the commission business by himself.

Q. And was that a business of some considerable size? A. His?

Q. At that time, his business?

A. It was growing. It was in its first year, as I recall it.

Q. Now after you set up your trust at first and the special partnership with yourself as general

(Testimony of Thomas H. Brodhead.)

partner and Mortimer Glueck and Bishop Trust Company, Limited, as special partners, after that was done were you called by counsel and advised anything about taxes?

A. I don't quite understand; immediately after this was formed?

Q. No, at sometime after you had formed your partnership and had set up this trust, sometime after that. A. Yes.

Mr. Nyquist: Your Honor, I would like to ask petitioners' counsel to refrain from leading questions at [28] this point.

The Court: Yes, very well.

Q. (By Mr. Wild): And what resulted from that contact, and about when was it, if you recollect?

A. It was approximately four or five months after the Thomas Holmes Brodhead trust was et up. Counsel called me and told me that the trust was, as a result of a Supreme Court decision as I remember it, was liable for the entire taxes, that I was responsible for the entire taxes of the trust and of the entire profits of the business, let's put it that way, and I asked, not knowing too much about it, what that meant, and it was found that—or I found out that if I had to pay the entire income taxes on the entire business, the profits of the entire business, I wouldn't have anything left, because I would still have to pay 50% to the special partner on all the profits and still pay all the taxes, and that was impossible.

(Testimony of Thomas H. Brodhead.)

Q. What did you do then? Did you consider that problem?

A. Most certainly. I asked what I could do about it, as I couldn't continue on that way. So I went to counsel for advice, and I was informed that I could either buy out the special partner or another trust could be set up at that time.

Q. Was anything said about your power of termination of the partnership business upon notice being given?

A. As I understand it, in the original trust, that I can [29] terminate it on sixty days' notice.

Q. Wait a minute, in the original trust?

A. The Thomas H. Brodhead trust.

Q. In the trust or the partnership?

A. In the partnership.

Q. Is there any such provision as that in the Thomas Brodhead trust? A. No.

Q. Very well. Now was any consideration given by you to the possibility that you might terminate the partnership?

Mr. Nyquist: Your Honor, I object to that question as leading.

The Court: I will ask counsel to avoid leading.

Mr. Wild: Very well.

Q. (By Mr. Wild): Recount all the factors that were considered when you were faced with the prospect of having to pay all the taxes on the total business income and only get half of the income.

A. Well, when that was pointed out to me that I would end up with nothing, in fact be in the hole,

(Testimony of Thomas H. Brodhead.)

that isn't business. I couldn't afford to do that. If I discontinued the partnership or bought it up entirely, I would be right back to where I started, and I had just gotten started under the new setup and was very happy, and I asked what could be done to continue it as is and still everything be on the [30] up and up, if you want to call it that, proper.

Q. And as a result of that, did you discuss anything with any representative of the Bishop Trust as well as Mortimer Glueck?

A. I discussed it with Mr. Glueck, because I went back to the office and he was the first one I saw, and after further consultation with him I came back and saw Mr. Cades. I do not recall whether I saw Mr. White or not.

Q. Did you discuss this at all with your wife at that time? A. I did.

Q. Now as a result of these discussions, what did you do?

A. Counsel advised me that another trust could be set up eliminating certain things in the Thomas Brodhead trust which had been ruled on by the Supreme Court, and upon counsel's advice a second trust later known as the Elizabeth Brodhead trust was formed.

Q. Did you participate in the formation of the second trust?

A. As advisor—would you state that in another way?

Q. Very well, did you contribute anything to

(Testimony of Thomas H. Brodhead.)

your wife as the starting capital of the second trust?

Mr. Nyquist: I object to the leading question.

The Court: Overruled.

Q. (By Mr. Wild): You may answer the question.

A. As I recall, I gave my wife $10,000 and paid the taxes [31] thereon to her.

Q. What do you mean by paid the taxes thereon?

A. It was reported as gift tax.

Q. I see.

A. I paid the gift tax I remember on $10,000 which I gave her.

Q. And what was that sum used for, if you know?

A. It was used as her down payment on the purchase of the Thomas Brodhead trust.

Q. What did it purchase from the Thomas Brodhead trust?

A. The 50% interest in the trust, the special partner's 50% interest in T. H. Brodhead Company.

The Court: What do we have here? Do we have two trusts in this case?

Mr. Wild: Yes, your Honor.

The Court: After she purchased the interest, does the old trust continue?

Mr. Wild: Oh, yes, both trusts continue and their accounts are in the record, your Honor, with substantial increases.

Q. (By Mr. Wild): In the Elizabeth Brodhead

(Testimony of Thomas H. Brodhead.)

trust after that was formed, was the partnership then changed?

A. There was no change in the operation of the partnership except that there was another trust set up as a special partner. That was all, if that is what you mean. [32]

Q. And then after the Elizabeth Brodhead trust became the special partner, who managed the partnership business of Thomas Brodhead and Company? A. I did.

Q. And did you or did you not receive special compensation for your services? A. I did.

Q. And what was the amount of that compensation which you received, first for the fiscal period from October 1, 1942, to the end of February, 1943?

A. In that fiscal year I received $6,250 as salary.

Q. And how was that used in computing the profits of the partnership?

A. That was paid to me first the same as any other employee in the concern, and then after all expenses including my salary and the rest of the employees' salaries, then the profits were divided.

Q. And what amount did you receive for the period from March 1, 1943, through February 28, 1944? A. Fifteen thousand dollars as salary.

Q. And the same question for 1945?

A. Eighteen thousand dollars.

Q. And the same for 1946?

A. Eighteen thousand dollars.

Q. And 1947?

A. Eighteen thousand dollars. [33]

(Testimony of Thomas H. Brodhead.)

Q. And 1948?

A. There Ace Distributors was formed, and T. H. Brodhead Limited and from Ace Distributors I received $9,000.

Q. And what did you receive from the corporation?

A. As I recall, $9,000. The business was split and my salary was split.

Q. Did you yourself consider these salaries concerning which you have testified as ample compensation for the value of your own services to these businesses? A. I did.

Q. During that time? A. Yes.

Q. Mr. Brodhead, during all of the periods of time from the formation of the special partnership down to the present time, who has paid for the living expenses of your children and your wife?

A. Myself alone.

Q. And out of what moneys?

A. Moneys that I have earned.

Q. Did you receive any moneys from the trust, your trust, the Thomas Brodhead trust?

A. No, and none were ever requested.

Mr. Wild: I think the Ace Distributors change is all stipulated, the time of it and all that. I think all that is in the stipulation. [34]

The Court: Was there a new partnership organization at the time of the Elizabeth Brodhead trust?

Mr. Wild: They went through all the steps essential to amending the old special partnership under our Hawaiian statute and changing that, sub-

(Testimony of Thomas H. Brodhead.)

stituting the new special partner for the old special partner so that there was no change there. Then later on the name, as shown in the stipulation, the name of the Thomas H. Brodhead Company special partnership was changed to Ace Distributors. That was at the time when they turned over half of the business shown in the stipulation to a new corporation, half of the stock went to the Elizabeth Brodhead trust and the other half went to the other partner.

The Court: Is that shown here in this stipulation?

Mr. Wild: Yes, it is in the stipulation.

The Court: The new partnership, so to speak.

Mr. Wild: Yes, it is not really a new partnership under our concept of the law here, your Honor. We have a special partnership law in which a special partner may buy the interest of another and if it is agreeable then there is a substitute in that same old special partnership.

The Court: Sort of uniform partnership?

Mr. Wild: Well, our special partnership act was later supplanted by the uniform partnership act. In 1943 [35] it became effective, but prior to that time under our law we had what was known as a partnership act providing for special partnerships.

The Court: But I mean one way you can convey an interest and it continues.

Mr. Wild: Well, you have to file your various

(Testimony of Thomas H. Brodhead.)
papers in the Treasurer's office, and upon such filing it continues right on, your Honor.

The Court: Very well.

Q. (By Mr. Wild): Now after Mortimer Glueck and Bishop Trust Company, Limited, became special partners in Thomas Brodhead Company, the partnership, did you consult with them as special partners?

A. I did. I always considered that I had—there were two people in the business, the special partner and myself, and it has always been operated that way.

Q. And how often would you have conferences with one or the other of the trustees, who were special partners?

A. Well, Mr. Glueck was in the same building with me. It was every day or every couple of days, several times a week, as things turned up. Later when he moved to the Bishop Trust Building, I would go over and see him. I also, at the same time that the partnership was formed, took on Cameron and Johnstone as my accountants. He was on the same floor with them, and I went over there very often to Cameron [36] and Johnstone, and I would stop in and see Mr. Glueck and go down to the Bishop Trust Company's office and see Mr. White and tell him how things were going along. And every time a financial report was put out, I always immediately went over there and discussed it with them and left them a copy of it.

Q. Now you mentioned Mr. White. Was there

(Testimony of Thomas H. Brodhead.)

any other officer of Bishop Trust Company that you consulted in connection with this special partnership business?

A. When Mr. White was not there, Mr. Benner would answer the questions. However, I usually found Mr. White in. If he was not, I saw him the next time that I was there when he wasn't busy.

Q. Did you have similar conferences after Mr. White left with Mr. Benner?

A. I absolutely did, in fact more so because times became more troubled and I had even more with Mr. Benner.

Q. And the times you had these conferences with Mr. White did Mr. Benner join in them sometimes?

A. It was with them that I had the conferences.

Q. Well, perhaps I misunderstood your answer to my first question and that was that you had spoken with Mr. White in the Bishop Trust Company. At that same time did you speak with Mr. Benner on frequent occasions?

A. Not so much with Mr. Benner because Mr. White was [37] the number one man. Mr. Benner's desk was right next to him.

Mr. Wild: No further direct.

Cross Examination

Q. (By Mr. Nyquist): Mr. Brodhead, I believe you stated on direct examination that Mr. Glueck had opened up your original set of books and grew up with your company. Can you tell us about when that original set of books was opened up?

(Testimony of Thomas H. Brodhead.)

A. As I recall, I started in business here in 1935 and he set up my original books.

Q. Had you been in the islands before 1935?

A. In 1934 I originally came here.

Q. Did you know Mr. Glueck before you came here? A. I did not.

Q. But you have known him since 1935?

A. Yes, because we were roommates together in a rooming house, I guess you would call it, at Pua-Lei-Lani at Waikiki Beach.

Q. You shared your living quarters with him at that time, is that correct?

A. We did.

Q. And his office was near your office, was it?

A. He was working right down the street here at a butter and egg concern. I have forgotten the name, and I was over here on Kaahumanu Street, about five or six blocks away. [38]

Q. It was close enough that you could get together frequently for lunch, was it? A. Yes.

Q. And during this period you would frequently get together for lunch? A. Which period?

Q. The early years from 1935 to the start of the war, let us say.

A. No, may I say no to that question and explain? During those years I was working during the daytime, I was out at Pearl Harbor working from morning to night, and even when I started the business when Mr. Glueck was first with me, and he moved out because of the fact that I stayed up all the time working in the room. He would

(Testimony of Thomas H. Brodhead.)

come in and I would be burning the lights and he couldn't go to bed.

Q. I believe you testified on direct examination that about this time in 1941 or 1942 you began to consider the business too risky to continue it as an individual. Will you explain just what you meant by that?

A. Yes, if I may go back. I started in this business—let's put it this way: There were four destroyers out here and a submarine. Later there were eight. Then it jumped when the Hawaiian detachment came here, which was a part of the fleet, and then it jumped some more. Then, if you will recall, the fleet was stationed here just before the [39] war. They only came over for maneuvers, and suddenly without notice they stayed, and that pushed the business up, and when you have an entire fleet calling on you for deliveries, because the ships order direct from us, and we had to work night and day. I had to expand quarters. And then the war came along, and you didn't know here what was going to happen at any time, and it got up into figures where even I couldn't realize that they had grown so fast and so big. I couldn't keep track of them.

Q. But when you say it was risky, you mean it was subject to fluctuations up and down depending upon such things as the number of men the military had stationed here?

A. Not so much that as that you were buying things on the mainland, fluctuations in market conditions, bringing them over here during the war

(Testimony of Thomas H. Brodhead.)

times, especially when they had convoys. You had accounts outstanding on ships that I didn't know what would happen, went down or sunk at sea, because our accounts were with the ship.

Q. In other words, you regarded the business as somewhat speculative or risky?

A. I had confidence in the navy, but what if ships went down and couldn't pay their bills, would I get my money back? I had so much confidence in it that I extended credit to the ships even after the war started, because I felt it was a patriotic and necessary thing to do, as I [40] was part of it.

Q. I understood you to testify on direct examination that it was because of this business risk that you decided to set up the trust.

A. It was more than I felt that I could handle. There were too many problems coming up. There was a problem of accounting. Mr. Glueck wanted to get out of that. There was a problem of buying. There was a problem of getting merchandise over here. There was the help problem.

Q. Which of these problems would the trust take over?

A. The general advising, where I could go to them and tell them the situation and what I wanted to do and whether I was right in that way of going about it. I also took on Cameron and Johnstone, which was a big help too, especially on the accounting end.

Q. Did the trust employ any people for your firm? A. Do what?

(Testimony of Thomas H. Brodhead.)

Q. Did the trust employ any people, handle any of your employment problems?

A. They hired none of the personnel.

Q. Did they do any of the accounting work for your firm?

A. Cameron and Johnstone did that.

Q. Did they do any of the buying for your firm?

A. They did not.

Q. Did they do any of the selling? [41]

A. They did not.

Q. You say at the time you decided some change should be made in your business you consulted an attorney. Who was the attorney?

A. Milton Cades.

Q. Is he the same attorney that you consulted in connection with the establishment of the Elizabeth Brodhead trust? A. He is.

Q. At the time the first trust was set up, the trust agreement which is exhibit one in this proceeding states, "The Settlor, in consideration of the love and affection he bears to the beneficiaries and of the acceptance by the trustees of the trust herein created, does hereby transfer, set over and deliver to the trustees, their successors in trust and assigns, the sum of $40,000." At that time was any cash actually transferred?

A. No, there was not, as I recall it.

Q. And at the time the Elizabeth Brodhead trust was created and I read from Exhibit five, "The settlor, in consideration of the love and affection she bears to the beneficiaries and the acceptance

(Testimony of Thomas H. Brodhead.)

by the trustees of the trust herein created, does hereby transfer, set over and deliver to the trustees, their successors in trust and assigns, the sum of $10,000." Do you know whether that was actually in cash?

A. I do not. [42]

Mr. Nyquist: May this document be marked Respondent's Exhibit A for identification?

The Court: Very well.

(The document referred to was marked Respondent's Exhibit ,'A" for identification.)

Q. (By Mr. Nyquist): Mr. Brodhead, I show you Respondent's Exhibit "A" for identification, a document entitled Gift Tax Return for the Calendar Year 1943, showing donor Thomas H. Brodhead, and ask you if that is the return which you filed for the year 1943?

A. That is the return that was made up by the accountants, by my accountant, the accountants for the business, Cameron and Johnstone, and that is my signature.

Q. I asked you whether that is the return that you filed for the year 1943?

A. That is the one that Cameron and Johnstone made up for me, evidently for 1943, and I have signed it.

Q. It shows over here "Received by Collector of Internal Revenue March 15, 1944." Did you file it with the Collector, or did someone file it on your behalf?

A. Cameron and Johnstone filed it for us.

(Testimony of Thomas H. Brodhead.)

Mr. Nyquist: I offer in evidence Respondent's Exhibit "A" for identification.

Mr. Cades: No objection.

The Court: Received. [43]

(Respondent's Exhibit "A" for identification was received in evidence as Respondent's Exhibit "A.")

Q. (By Mr. Nyquist): Now I show you on the reverse side of Exhibit "A" a description of a gift to Elizabeth Brodhead on February 28, 1943, in the amount of $10,000.00, and I note under there the word "Cash" appears. Do you know for sure whether cash was in fact given at that time?

A. I do not.

Q. Do you have any recollection of giving a note in the amount of $10,000 at about that time?

A. I do not.

Q. Going back to the time that you set up the Thomas Brodhead trust, did you know any other people who set up similar trusts at about that time?

A. No. I did have a cousin in Hilo who had had a trust for her personal property, however.

Q. But did you know any other individuals who set up trusts and made the trusts members of partnerships at that time?

A. No, I did not, that I recall.

Q. Now at the time you created the Thomas Brodhead trust, you put in that trust instrument a provision that the trustee should contribute the sum of $40,000 to the capital of the partnership known as the T. H. Brodhead Company for a 50% interest

(Testimony of Thomas H. Brodhead.)

therein, and the statement appears, "Said sum [44] being a fair and reasonable value of said interest duly ascertained as of September 30, 1942." Can you tell me what you mean by that statement, "Said sum being the fair and reasonable value of said interest"? In other words, how did you determine the fair and reasonable value of said interest?

A. Cameron and Johnstone took over the books immediately the partnership was formed. Mr. Glueck before that, I believe, had brought the books up to date as of the end of September, or whatever date it was, and when it was formed the value of the company, or my business at that time—it was then known as T. H. Brodhead—was approximately $80,000.

Q. In other words, when you use value there, you are referring to the book value as it appeared on your books at that time, is that correct?

A. I am putting it as cost of merchandise, accounts receivable, payable, everything taken into consideration as to the value of the business at that time.

Q. And the physical assets at their depreciated value on your books?

A. That is an accounting question that I could not answer.

Q. Did you take into account any good will that the business might have had at that time? [45]

A. I did not.

Q. But the business was relatively prosperous at that time, was it not? A. Yes, it was.

(Testimony of Thomas H. Brodhead.)

Q. And did you consider it had a going concern value over and above the value of those fixed assets?

A. In those days you couldn't contemplate anything because the war had just begun and we were still in a very unsettled condition here.

Q. Would you have sold a 50% interest to an outsider for $40,000?

A. No. I wouldn't have sold.

Q. Now I show you Exhibit four, entitled a Certificate of Special Partnership and affidavits which affidavit was signed by you as a general partner, and it has been stipulated that that document was filed with certain local governmental officials. Will you tell us what the occasion was for your signing that document?

Mr. Wild: Might I ask what the purpose of this is? This is stipulated in the record as having been filed, and if that is the evidence, I don't know what the purpose is.

Mr. Nyquist: This is cross examination, your Honor. I am asking him what his purpose was.

Mr. Cades: It is stipulated it was filed as [46] required by law.

The Court: Overrule the objection. Can you answer the question? Do you know why?

The Witness: It says here it was filed in the Treasurer's office, and I imagine it means that it is a certificate of partnership which they have to file here in the Territory.

Q. (By Mr. Nyquist): Let me ask how did you

(Testimony of Thomas H. Brodhead.)

happen to file it? Did you know it should be filed?

A. I did not. I was advised by counsel.

Q. You were advised by counsel, Mr. Cades?

A. Either Mr. Cades or Cameron and Johnstone. I don't remember which. I relied on them for business details of that type.

Q. Now at the time that the Elizabeth Brodhead trust was created, I believe that on direct examination you testified that it was created because you found you had some sort of a tax problem and you were advised that this was a solution to the problem. Will you explain just how you understood the Elizabeth Brodhead trust was to solve your tax problem?

A. As I understood it, the Thomas Brodhead trust allowed certain moneys to be paid out to the children in case—for their maintenance and support and education in case of necessity. In other words, if I went broke or anything like that, died, something like that; and that a Supreme [47] Court decision had ruled it as making me personally responsible for all the income, and that by setting up a new trust eliminating that, which would make it so that I could not have anything to say, do or anything else with the new trust, that everything was in the entire hands of the trust company.

Q. Well, what was to happen to the Thomas Brodhead trust after the change took place, after the new trust was created?

A. That was to remain as it was, two separate entities.

(Testimony of Thomas H. Brodhead.)

Q. Wasn't it your understanding that the income of that trust would still be taxable to you?

A. I believe at that time the trust—that had all been arranged for, the payment of the taxes on that. This had only gone for four or five months. I mean, it was practically overnight.

Q. Let me ask you this: When the Elizabeth Brodhead trust bought the partnership interest from the Thomas Brodhead trust, what did the Thomas Brodhead trust do with whatever it received as consideration?

A. That was in the trust company's hands. I had nothing to say about that. I am only the general partner and half owner in the business.

Q. Did the Thomas Brodhead trust loan $10,000 to your business immediately after the creation of the Elizabeth Brodhead trust? [48]

A. I don't know. I do not recall. I was too busy making sales and getting merchandise to take care of bookkeeping details.

Q. Did you believe that the sale of this interest to the Elizabeth Brodhead trust would leave the Thomas Brodhead trust without assets?

A. No.

Q. Did you believe that the Thomas Brodhead trust would have assets that would be invested and receive income on?

A. It was a debt owed. It was a debt, I mean on the books of the company. It was there.

Q. What was the debt on the books of the company, a debt to the Thomas Brodhead trust?

(Testimony of Thomas H. Brodhead.)

A. The $40,000.

Q. What $40,000?

A. The original investment of the special partner, and all the earnings for that five-month period were the property of the Thomas Brodhead trust.

Q. Yes, but originally when you set up the Thomas Brodhead trust, you stated in the trust agreement that it had a $40,000 gift to start with. What happened to that $40,000?

A. What happened?

Q. Yes.

A. It is all in the Thomas Brodhead trust.

Q. And what did you contemplate that the trustee would do [49] with that $40,000 after the creation of the Elizabeth Brodhead trust?

A. Invest it.

Q. Invest it; and did you contemplate that they would receive income on it?

A. A certain amount, yes.

Q. And since you were aware of the Supreme Court decision which you thought made you taxable on the income of that trust, didn't you expect to have to pay an income tax on whatever income that trust had? A. No.

Q. Why not?

A. Because that was already formed, money paid in. I mean that was on their books as their property and not mine from there on.

Q. Well, let's put it this way: Did you expect that whatever investments that the Thomas Brodhead trust might make would produce income in

(Testimony of Thomas H. Brodhead.)

amounts comparable to the 50% partnership interest profits?

A. I am a little confused on the question.

Q. Let me rephrase to make it clearer.

A. Yes.

Q. During the first year of its existence, the Thomas Brodhead trust showed a distributive share of income from the T. H. Brodhead Company of $36,681.45. [50] A. It showed as what?

Q. The Thomas Brodhead trust showed that as its distributive share of the income from T. H. Brodhead Company for the fiscal year ending September 30, 1943. Now did you believe that the income of the Thomas Brodhead trust would continue to be that high, or that it would be a lesser amount after the creation of the Elizabeth Brodhead trust? A. Well, it would be much less.

Q. Much less. Why would that be?

A. Well, normal stocks and bonds do not pay that much interest.

Q. You mean the same amount of money invested in other places you wouldn't expect to produce income in anywhere near that amount, is that correct? A. Yes.

Q. How many children did you have at the time this Thomas Brodhead trust was created?

A. One and the possibility of another one.

Q. As I understand, one of your purposes in creating the trust, you state, was to provide for your children in the event something should happen to you, is that correct?

(Testimony of Thomas H. Brodhead.)

A. That is correct.

Q. Did you make any similar provision for your wife? A. No.

Q. Why was that? [51]

A. Well, I had insurance to take care of her.

Q. We have spoken about investments made by the Thomas Brodhead trust after it sold its interest in the partnership. Did the trustee consult with you, or did you consult with the trustee about the investments which the trust made?

A. The trustee would show me a list of what their investment department recommended and ask my consideration of same.

Q. And then did you signify your approval of certain investments?

A. I did.

Q. And after that the trust would make the investment that you had approved, is that correct?

A. That is correct. They approved them. That was their prerogative.

Q. In other words, you both approved them?

A. We both approved them. Mr. Glueck, I believe, had to approve them too.

Q. Was that also true of the other trust?

A. The Elizabeth Brodhead trust?

Q. Yes. A. I don't know.

Q. Did you ever discuss with the trustees the investment of the Elizabeth Brodhead trust?

A. I have not, as I recall. [52]

Q. Did you ever discuss with your wife the investments of the Elizabeth Brodhead trust?

(Testimony of Thomas H. Brodhead.)

A. I have. I discussed my business problems with her at all times. Let's put it that way.

Q. Did you advise her on such investment matters?

A. No; the same as with the Thomas Brodhead trust, a trust company where their department knows a lot more about investments than I do. I am a greenhorn. The only thing to do is to take the advice of experts on it. That is their business, not mine.

Q. Therefore, you just adopted their recommendations, is that true?

A. One request I made was that they consider the investments not from a return for them but a safety of investment, and at one time I did ask that government bonds be purchased rather than other types of stocks. That was my request at one time, and another time was a certain local stock had gone down and I requested that when it went up again that it would be better, that I would recommend that they sell it out and get into something more on a national scale, on a larger scale, rather than a local scale.

Q. Did the trustees consult with you on occasions about withdrawing their share of the partnership profits from the business?

A. They did. [53]

Q. Did they frequently make requests of you for money to be used to pay trust taxes?

A. They did.

(Testimony of Thomas H. Brodhead.)

Q. And after such requests you would distribute the money to them? A. That is correct.

Mr. Nyquist: I have no further questions, your Honor.

The Court: Is that all the money that was distributed? That is, you just gave the trust enough to pay the taxes and left the rest in the business?

The Witness: No. As of today 50% of everything has been distributed to the trust company. The Ace Distributors end has all been settled up. There is $5,900 in the bank, of which $2,500 is the Elizabeth Brodhead trust's, and the remainder belongs to me. But the rest has been straightened out, and the Ace Distributor's end is practically wiped out. Brodhead Company, Limited, is still in operation, and after about three years of hard going, as of February 28th the assets are over the stock value and business since then has been much better.

The Court: Have you some further inquiry?

Mr. Wild: I beg your pardon, your Honor?

The Court: The government is through. Do you want to ask some more questions? [54]

Mr. Wild: Yes, your Honor.

Redirect Examination

Q. (By Mr. Wild): Government counsel asked you if you had protected your wife in this deed of trust. As I understood it you said no, and then you said you had her protected by insurance. Did you also at that time have a will? A. I did.

Q. And was your wife provided for in that will?

(Testimony of Thomas H. Brodhead.)

A. She was. We had our wills drawn at the same time, leaving in case of separate deaths one to the other, and in case of both dying at the same time, in a plane crash, let's say, that everything would go to the children, but Bishop Trust Company was made executor in all three instances. They were identical or tied in to work together.

Q. And another question, you stated a few moments ago two things that you requested the trust company to consider in regard to investments. Did you also request them to purchase a specific stock?

A. No, not that I recall.

A. A publishing company stock?

A. Oh, I will take that back. The answer is yes, and I will explain it. When my mother died she left me some Knight Newspaper stock, and it was a concern that my father was—originally helped get on its feet. Mr. C. L. Knight was [55] his personal friend, and he was advertising manager of the original newspaper. It paid very good dividends and still does. I took that to them and asked them if they would be interested in purchasing that at what I inherited it, the book value, the assessed value, and that it would pay a good dividend for them, and it would be protected in the family for my children. Mr. Benner said he would look it up. He came back later and said no, that they refused to purchase it because of the fact that it was a family corporation and wasn't listed on the stock exchange so that it could be bought and sold at any time, so I still have it.

(Testimony of Thomas H. Brodhead.)

Q. Mr. Brodhead, did you try to tell the trust company how to operate that trust at all?

A. Absolutely not.

Mr. Wild: No further questions.

Mr. Nyquist: Before this witness leaves the stand, your Honor, I would like to offer in evidence as Respondent's Exhibit next in order the consent waiving the period of limitations upon the assessment for the year 1943 signed by Thomas Brodhead and Elizabeth Brodhead.

Mr. Cades: No objection.

The Court: Received in evidence.

The Clerk: Exhibit B.

(The document referred to was received in evidence as Respondent's Exhibit "B".) [56]

The Court: Is that all?

Mr. Nyquist: Yes, your Honor.

The Court: You may step down.

(The witness was excused.)

The Court: We will take a brief recess.

(Recess.)

Mr. Wild: Mrs. Brodhead, will you take the stand, please?

ELIZABETH S. BRODHEAD

Petitioner, called as a witness in her own behalf, being first duly sworn, was examined and testified as follows:

The Clerk: Will you please state your name and address for the record?

(Testimony of Elizabeth S. Brodhead.)

The Witness: Elizabeth S. Brodhead. The address is 1468 St. Louis Drive.

Direct Examination

Q. (By Mr. Wild): Are you the Elizabeth S. Brodhead who is co-petitioner in docket number 29391 and docket number 29392? A. I am.

Q. And you are the wife of Thomas Brodhead?

A. Right.

Q. Who was just on the stand? A. Yes.

Q. And do you remember an occasion when you discussed the [57] possibility of the formation of a trust for your children?

A. I can't give you any definite dates for that, but I know that we talked about it at home.

Q. About when was it, if you recollect, sometime in 1943 or when?

A. I don't remember exactly. Perhaps the first of 1943, January perhaps, sometime, I would say, after the first of the year.

Q. Sometime after the first of the year in 1943?

A. 1943, yes.

Q. And what, if anything, resulted from those conversations?

A. I went to see counsel to see whether I could establish a trust for the children. I suppose I wanted a chance to play Santa Claus like my husband.

Q. I can't hear.

A. I went to counsel to see if I could set up a trust for the children as my husband had done. I

(Testimony of Elizabeth S. Brodhead.)

thought perhaps I could play Santa Claus to the children.

Q. Where were you to get the funds which were to be used to start this trust?

A. My husband has always trusted me with his salary, and he said that he would give me $10,000 if I wished to do it.

Q. I see. And did you discuss the terms of the trust instrument with anybody? [58]

A. I discussed it with the attorney. I don't think that my husband went with me to the attorney's office when I talked to him about it. I talked to my husband at home.

Q. Well now, did you know the terms of your husband's trust?

A. Yes, indeed. I had heard all of that discussed before he established it.

Q. I see. Were there certain differences in the trust that you wanted to create?

A. I felt it would be better if the children didn't get so much money at one time, that is if I could set it up so they would get the results of my trust over a longer period it would be better.

Q. A longer period than what?

A. As it happens, the trustees can disburse the trust, I believe, beginning from the time they are twenty-one, and mine was left so that they would get $10,000 from the time the youngest was twenty-three, and after five years she would get—I don't mean she got that much. The three children would get what had accumulated when the youngest was

(Testimony of Elizabeth S. Brodhead.)

twenty-three and it could not be more than $10,000. There was that limit, and when the youngest was twenty-eight another distribution could be made, not to exceed $10,000, and when the youngest is thirty-three the final distribution would be made, which as it turns out would [59] mean that the eldest would be thirty-eight and one-half. I think she should have wisdom enough to use the money better at that age.

Q. Whose determination and decision were those provisions? A. They were mine.

Q. In that respect the trust differed from the one your husband had set up?

A. The trust differed, yes. The trustee was the same.

Q. The trustees in your trust, did you speak with them?

A. I can't remember whether I spoke to them before it was set up or not. I remember telling Mr. Benner that I hoped he would be the one the Bishop Trust would put in charge of my trust, but I don't think I conferred with him. I went to counsel.

Q. I see, and what about the consideration for the purchase of the partnership interest of the Thomas Brodhead trust? Who was that taken up with? A. You mean the $10,000?

Q. No. You considered whether or not the trust wanted to purchase or did want to purchase the interest in the special partnership owned by the Thomas Brodhead trust, did you not?

A. I asked my husband, naturally, if it would be with his approval that another trust be set up

(Testimony of Elizabeth S. Brodhead.)

to take over the 50% interest in his company. Naturally I wouldn't want to [60] do that behind his back.

Q. And did you also take that up with the trust company?

A. I can't remember that.

Q. You don't remember that?

A. I don't remember that.

Q. Well now, as a result of that, you executed a deed of trust which is in the record.

A. Right.

Q. And you desired your trust to purchase a half interest in the partnership?

A. That's right.

Q. That had been owned by the Thomas Brodhead trust? A. Yes.

Q. Do you know whether that was accomplished, in fact?

A. I believe it was. The trustees have given me an annual report every year for my information.

Q. Now who was the manager of the Thomas Brodhead Company, the co-partnership?

A. My husband, Thomas H. Brodhead.

Q. And during the period of time after the establishment of your trust to the present, has your husband attempted to dictate to you as to any policies of investment in your trust? A. No.

Q. Have you attempted to dictate any policies of investment [61] to the trustees under your trust?

A. No. I think the same stipulation is in my trust that is in the Thomas Brodhead trust that while I am living I can be notified of the invest-

(Testimony of Elizabeth S. Brodhead.)

ments, I should be notified of the investments. That has occurred only once, last year.

Q. Now do you know whether the Elizabeth Brodhead trust has substantial assets at the present time?

A. Yes, the last statement that I saw was favorable.

Mr. Wild: No further questions.

Cross-Examination

Q. (By Mr. Nyquist): Mrs. Brodhead, you testified on direct examination about getting this impulse to play Santa Claus and setting up a trust for your children. Did you ever set up any trusts prior to that time? A. No, I never had.

Q. Have you set up any since? A. No.

Q. Well, will you explain just what the circumstances were that led to your getting this impulse right at that time?

A. As has been shown before, the arrangements whereby the Thomas Broadhead trust was set up meant that we perhaps were going to lose everything that he had hoped to give the children, and it seemed to me that by a perfectly legal and correct procedure I could not take away anything, that [62] had been given to them, but to increase what had been given to them.

Q. Where did you get this information from, Mr. Brodhead or whom?

A. Probably some from him. Mr. Glueck sometimes came to the house, and any men that came to

(Testimony of Elizabeth S. Brodhead.)

the house would discuss business, so I would hear it from probably several people.

Q. Well, how did the first action start when it came down to creating this trust, the decision to create it? Did you figure out the idea of setting up another trust?

A. I went to Mr. Cades and asked whether I could do it, how I could do it.

Q. You mean you had the idea of setting up the trust first and then you went to Mr. Cades?

A. Well, yes, I wouldn't go to him unless I had the idea.

Q. Where did you get the idea?

A. I discussed—probably came partly from my husband and partly from any other men that had been talking about the problem.

Q. You had been talking about it with your husband?

A. Yes, we talk business a great deal.

Mr. Nyquist: Your Honor, I wish to introduce at this time the gift tax return of Elizabeth Brodhead for 1943 as Respondent's Exhibit next in order.

The Court: It will be received. [63]

The Clerk Exhibit C.

(The document referred to was received in evidence and marked Respondent's Exhibit "C".)

Q. (By Mr. Nyquist): Mrs. Brodhead, I show you Exhibit "C" which is a gift tax return for the calendar year 1943, which is signed by you and

(Testimony of Elizabeth S. Brodhead.)

filed with the Collector on March 1, 1944. Now turning over to the reverse side of this is a description of gift, and under the printed words description of gift and donee's name and address there are typed these words, "To Mortimer Glueck and Bishop Trust Company, Limited, trustees under deed of trust of Elizabeth S. Brodhead dated February 28, 1943," and the address is shown, "Gift of cash to purchase capital interest of special partner in T. H. Broadhead Company". The date of gift is February 28, 1943, and the value is shown as $10,000. Now I am asking you do you recall the occasion of that gift, and tell us just what form that $10,000 took, whether it was——

A. You know, I think it was a check.

Q. You think it was a check?

A. I think it is the only time I have had a check of that value in my hands. That's why I feel that way.

Q. Do you recall definitely whether it was a check or a note?

A. No, I do not.

Q. At the time you created the Elizabeth Brodhead trust, did you carefully consider the provisions that appear in the trust instrument?

A. Yes indeed, I read it many times.

Q. And you have stressed in your direct examination the importance you attached to the difference in the dates upon which the children could receive any distributions from the trust. Did you consider it quite important that they not receive

(Testimony of Elizabeth S. Brodhead.)

their distributions before they reached the ages that are mentioned in the trust instrument?

A. In Mr. Brodhead's trust provision is made for their maintenance, I think, so that was covered fully, I thought, in his trust, and this is cash which they will get as adults.

Q. But my question is did you consider it quite important that they not receive any distribution until they attained the ages that were mentioned in the instruments? A. Yes, I do.

Q. Well then, will you explain just why you put in the provision that the trustee may terminate the trust at any time it seems best for him after the trust ceases to be a special partner in the T. H. Brodhead Company?

A. If my husband should die, the partnership would be dissolved, wouldn't it? Q. Yes.

A. And therefore the trust company would be able to dissolve the partnership and take their share and turn his remainder to me. Wouldn't that be the reason for it?

Q. I am asking you the reason for it.

A. I think that would be a time when it would be necessary for a terminus to be put on it.

Q. You say that you put that in because you wanted the trust to terminate in the event of the death of your husband?

A. Not necessarily that the trust would terminate, but that the business might have to be sold. I wouldn't feel myself capable of running his business.

(Testimony of Elizabeth S. Brodhead.)

Q. But I am asking you why you put in the provision that the trust could terminate?

A. My father is a lawyer, and I believe that all the legal angles should be covered from the beginning if possible, to avoid difficulty later on.

Q. I still ask why you think the trust should terminate?

A. I don't think it should terminate at all. I think it is in very good hands.

Q. Why did you put in a provision allowing the trust to terminate in the event the partnership should terminate? A. My opinion today?

Q. I am asking you your reason at that time.

A. I can't tell you what my definite feeling at that moment was.

The Court: Where is that provision?

Mr. Nyquist: That is at the end of paragraph D, your Honor, in Exhibit 5.

The Court: Is there a provision in this trust saying what will be done in that event?

Mr. Nyquist: Yes, in the event of the termination of the trust, the instrument provides that the trustee may pay the corpus and income to the parents of any minor beneficiaries.

The Court: To whom?

Mr. Nyquist: To the parents of any minor beneficiaries.

The Witness: I doubt that.

Mr. Nyquist: That appears in most of these, and I think it appears in this.

The Witness: I believe that is not in it. I be-

(Testimony of Elizabeth S. Brodhead.)

lieve it says the money shall be divided among the children and in case the children all die the property shall revert to the next legal heirs, but excluding the grantor and her husband.

Mr. Nyquist: I read from Paragraph J, your Honor, "If any person entitled to receive any of the income or capital of the trust estate shall be a minor, the trustee may pay the share of income and capital to which said minor is entitled to either parent," and so forth.

The Court: What I was inquiring primarily about is this: Is there a provision in this instrument that the [67] trust terminates at any time that the partnership terminate?

Mr. Cades: No, there isn't.

The Court: What does that provision mean that counsel read?

Mr. Cades: It provides that the trustee may terminate the partnership within one year after the partnership ceases to be a partner.

The Court: After the trust ceases to be?

Mr. Cades: After the trust ceases to be. The reason for that, if the Court will take my statement on the matter, is that the trust company insisted on that, because it was the only asset of the trust, and they did not know whether the assets would be of any significance and they wanted an opportunity to get out of what might be a non-profitable trust if the property in the trust didn't amount to anything.

The Court: Well, the proviso at the end of that

(Testimony of Elizabeth S. Brodhead.)

paragraph D says this, "Provided, however, that if not terminated prior thereto, the trustees may determine this trust at any time, but not more than one year, which to the trustees may seem best after the trust shall cease to be a special partner in the partnership known as the T. H. Brodhead Company". What does that mean?

Mr. Cades: That means that in the event that the trust shall cease to be a partner in the special partnership [68] the trustees have a one-year period within which to determine whether the trust shall continue or shall not continue.

The Court: But suppose they decide it shall not continue. What happens? It seems an odd provision to me, because they might sell an interest in the partnership and invest it in something else. I don't quite know why they have that.

Mr. Cades: In the event of the termination at any time, then the trustees are required to set over all the property to the children of the settlor then surviving the lawful issue of any of said children, or there being none then to those persons other than the settlor and Thomas Brodhead, husband of the settlor, who would be the heirs at law, of the last surviving of the settlor, under the statutes of the Territory of Hawaii in force and effect at the time of her death.

Mr. Nyquist: But in that connection, Provision J would come into effect, your Honor, which would allow the trustees to make the payments to the parents of any minor beneficiaries.

(Testimony of Elizabeth S. Brodhead.)

Mr. Cades: That is the usual law in the Territory, that the parents are the natural guardian, and payments may be made in any event. It is merely not on their own right; it is just the right to receive on behalf of the minor children. [69].

The Court: As a fiduciary?

Mr. Cades: That's right.

Q. (By Mr. Nyquist): Mrs. Brodhead, have you ever made a study of the investment market?

A. No, I took the Bishop Trust Company's course in finance, and they taught us to go to experts.

Mr. Wild: How long ago was that?

The Witness: That was last fall, but I believed it a long time before that.

Q. (By Mr. Nyquist): Then in approving any recommendations that were submitted to you for investments, did you make any independent decision of your own? A. No, purely technical matters.

Q. You mean you exercised no independent judgment in the matter?

A. No; as a matter of fact, I lost the letter and they had to phone me to send it back to them.

Q. Did you direct them?

A. No, I read the letter, and I noticed they were diversified. I believe it was five or six different items that they got at that time.

Mr. Nyquist: No further questions, your Honor.

Redirect Examination

Q. (By Mr. Wild): You had known Mr. Mor-

(Testimony of Elizabeth S. Brodhead.)

timer Glueck, the other trustee, [70] for some time?

A. Yes. Mr. Brodhead was here when I came over in 1938 to be married. I had known him on the mainland. I came over at that time, and I met Mr. Glueck probably in July, 1938, and I have always respected his judgment a great deal.

Mr. Wild: No further questions.

The Court: Step down, please.

(The witness was excused.)

Mr. Wild: Mr. Glueck, will you take the stand?

MORTIMER J. GLUECK

called as a witness in behalf of Petitioners, being first duly sworn, was examined and testified as follows:

The Clerk: Please state your name and address.

The Witness: Mortimer J. Glueck, 3189 Diamond Head Road, Honolulu, T. H.

Direct Examination

Q. (By Mr. Wild): Mr. Glueck, how long have you known Thomas Brodhead?

A. Since 1935, I believe, June of 1935.

Q. And during some period of that time, about when did you perform certain services for him?

A. Well, starting with that time Mr. Brodhead was just starting a business, practically a one-man business at that time, and I believe I started keeping his books, and I continued to do so in setting up his office and advising [71] him, well, right up to the present day.

Q. Well, do you keep his books now?

A. No, I advise him, but I do not keep his books.

(Testimony of Mortimer J. Glueck.)

Q. About when did you tell him that you would have to cease keeping his books?

A. I believe it was in the early part of 1942 when the war started. I went in as a volunteer in the military governor's office. I was working there all day and trying to do my business at night. And I was also in a military organization down here, a civilian military organization, and I just didn't have any more time. My business was expanding as well. I told him I thought it was wise to get a public accountant who would devote their time and not depend on my occasional assistance as the thing progressed.

Q. What other things were covered in your discussion with him at that time?

A. Just before the start of the war Mr. Brodhead's business began to build up. Prior to that time it was in its embryonic stages and gradually was building up, and I had discussed the question of setting up something so that in case of his death his children and his wife would have a continuing business. After the war started, Mr. Brodhead was rather obsessed with the fear of death, not the fear of death—let me put it this way— His father and grandfather both died as young men. Mr. Brodhead was then at that time [72] a year or two older, I believe, than his father or grandfather at the time of their death, and naturally the conditions here in Hawaii in early 1942 was not conducive to a feeling of long life, and he felt that there was a possibility he would not live too long in view of that. So we discussed the question of setting up a trust

(Testimony of Mortimer J. Glueck.)

and setting this trust up as a partnership so that in case he died the special partner could become a general partner and continue the business. And that was the point that we discussed with Mr. Cades when we went to him the first time in establishing the trust.

Q. Whose idea was the creation of this trust?

A. I believe it was my advice.

Q. Was that prior or subsequent to the time you saw Mr. Cades?

A. Oh, some time prior. I had a friend of mine, not a friend of mine, a fellow worker in 1928 who had at one time had a lot of money and went through it very rapidly, but some time during the course of that period he had set up an irrevocable trust for the benefit of his children, and I had always remembered how well he felt because despite the fact he didn't have a dime, at least his children's welfare was taken care of, and that was one point I had stressed to Mr. Brodhead.

Q. Now had you discussed with him any part that you might [73] play if a trust were set up?

A. No, I had not.

Q. You did not?

A. Whether if I were trustee?

Q. Yes, whether you would be a trustee or not.

A. Yes; sorry, I didn't understand.

Q. How had that come about?

A. He asked me whether I would be trustee, and I told him yes, and that if I were trustee in case of his death then I would be in a position with the

(Testimony of Mortimer J. Glueck.)

knowledge I had of his business to manage his business as the special partner.

Q. And was there to be another trustee? How did that evolve?

A. I recommended to Mr. Brodhead that a trust company be appointed as trustee. I am a few years younger than Mr. Brodhead, but I am still approximately his age, and my chances of surviving him was not considerable, and I thought it was unreliable to have an individual as a trustee.

Q. I see, and as a result of these conversations this Thomas H. Brodhead trust was set up and the partnership that is in the stipulation were all set up and operating? A. That's right.

Q. And do you know who was the manager of the partnership business?

A. The partnership has been managed by Mr. Brodhead. [74]

Q. During that period of time after the partnership was started had Mr. Brodhead consulted frequently or infrequently with you?

A. Well, particularly during the war years, very frequently.

Q. Now has Mr. Brodhead any control over your investment policies at all, any practical way of controlling your investment policies? A. As trustee?

Q. Co-trustee, yes. A. No.

Q. Do you feel under obligation to do for him exactly what he wants you to do?

A. No. On the contrary, I feel as a trustee under this trust deed my obligations are to the trust and

(Testimony of Mortimer J. Glueck.)

not to Mr. Brodhead, because it was clearly understood at the time the trust was signed that he was signing an irrevocable trust. He had nothing more to do with it.

Q. You were also a trustee, Mr. Glueck, of the Elizabeth S. Brodhead trust, I believe.

A. That is correct.

Q. And did you participate in the discussions that occurred prior to the time that that trust was set up?

A. I believe I did. I don't recall too well. The trust was set up following pretty much the same provisions as the original trust with a few exceptions that Mrs. Brodhead [75] requested, and I believe I attended one or two conferences with Mr. Cades on that.

Q. Do you have any clear recollection of what occurred at that time?

A. Not too clearly, no, sir.

Q. Not too clearly. Now during the intervening years up to the present time in the administration of the Elizabeth S. Brodhead trust have you had frequent consultations with the Bishop Trust Company, your co-trustee?

A. Yes, they do not take any action without giving me a letter and getting my signature consenting to that particular action, whether it be investment or what, and in addition to that, I am a personal friend of Mr. Benner, and I see him possibly at least every two or three weeks.

(Testimony of Mortimer J. Glueck.)

Q. And that same thing is true as co-trustee under the Thomas Brodhead trust?

A. That is correct.

Q. And in the administration of those two trusts with the Bishop Trust Company, do you feel that either of the settlors has any control over your actions as trustee? A. Absolutely not.

Mr. Wild: No further questions.

Cross Examination

Q. (By Mr. Nyquist): Mr. Glueck, have you ever had a legal education? [76]

A. Other than business law in college.

Q. As I understood your testimony on direct examination, you said the idea of setting up these trusts was your idea. A. That is correct.

Q. What was your reason for making the trust a limited partner?

A. Well, under the law as I believe—now I am not an attorney, so probably cannot answer this correctly—but this is my interpretation of the law. A limited partner, a special partner had a limited liability under a partnership. A general partner had an unlimited liability, and we didn't feel the trust should go into anything where they had an unlimited liability.

Q. Well, you say it was your suggestion that the trust be a limited partner.

A. May I correct you? It was my suggestion that the trust be a partner. The legal details were worked out by counsel, not by myself.

(Testimony of Mortimer J. Glueck.)

Q. But as I understand you, you say your purpose was so that you would be in a position to manage, take over the management of the business in the event of the death of Mr. Brodhead.

A. Well, the Bishop Trust Company and myself as co-trustees, yes.

Q. Did you study over the terms of the trust and the partnership agreement before they were signed? [77] A. Yes, sir.

Q. Did you realize that the trust was a limited partner? A. Oh, yes.

Q. Did you realize that the trust would remain a limited partner after the death of Mr. Brodhead?

A. Well, I believe there was some way of the trust assuming, I believe under the Territorial law, by merely taking action they become a general partner. The minute a special partner manages a business or takes any management steps, he becomes a general partner.

Q. That is your understanding of the Territorial law?

A. That was my understanding of the law, yes, sir.

Q. Was it your understanding it would become a general partner not only for the purpose of liabilities but for the purpose of assuming management powers?

A. That was my interpretation, but I am not a lawyer.

Q. It was your belief at the time that after the death of Mr. Brodhead the trust company would

(Testimony of Mortimer J. Glueck.)

be—the trust would be able to take active management of the business, is that correct?

A. That was the intent.

Q. Did you receive copies, as trustee, of either of these trusts? A. No.

Q. You stated that you regarded your obligations as being [78] to the trust and not to Mr. and Mrs. Brodhead. Did you consent to the sale by the Thomas Brodhead trust of its share in the partnership to the Elizabeth Brodhead trust? A. Yes.

Q. As trustee of the Thomas Brodhead trust, did you not regard your duty as to the beneficiaries of that trust? A. I do.

Q. Did you believe that after the sale of the partnership interest that you would be able to invest the trust corpus that remained in investments that would be as profitable to the trust as the partnership interest was?

A. Well, as I understood at the time, if we did not consent to the sale——

Q. I am asking you. Will you answer my question?

Mr. Wild: Let him answer.

The Witness: I am trying to answer, if I may.

The Court: You answer it and then explain it. Read the question, please.

(The question was read by the reporter.)

A. No, and may I explain that, your Honor?

The Court: Yes.

The Witness: As I understood at the time if we did not consent to the sale and the transfer from

(Testimony of Mortimer J. Glueck.)

the Thomas Brodhead to the Elizabeth Brodhead trust, that Thomas Brodhead would not be able to do anything else but dissolve [79] the partnership. Therefore, we would have no prospect of reinvesting in the partnership. Since my obligations are to the beneficiaries of the trust deed and they were to be the same under the Elizabeth Brodhead trust, I felt that I was doing my duty in consenting to the transfer.

Q. You mentioned the possibility of dissolution of the partnership. Would that have been a serious blow if that had happened?

A. Well, yes. The partnership at that time was making very very fine returns on their investment, and as I understood it at the time, the accountants explained Mr. Brodhead had to pay the full income tax of the partnership and only receive half of it. He actually would be paying out more than he was receiving and therefore could not continue.

Q. Well then, your purpose in consenting to the sale of the partnership interest to the second trust was to relieve Mr. Brodhead of his unbearable income tax burden, is that correct?

A. My interest was primarily in the benefactors under the trust deed. We wanted to retain in some way a very profitable investment.

Mr. Wild: Did you mean benefactors or beneficiaries?

The Witness: I think it is beneficiaries.

Mr. Nyquist: I have no further questions.

Mr. Wild: That's all. [80]

The Court: Step down.

(The witness was excused.)

Mr. Wild: Mr. Benner, will you take the stand?

EDWIN BENNER JR.

called as a witness in behalf of the Petitioners, being first duly sworn, was examined and testified as follows:

The Clerk: State your name and address, please.

The Witness: Edwin Benner, Jr., 4473 Aukai Street, Honolulu, T. H.

Mr. Wild: Government counsel are willing to stipulate the first eleven questions and answers, including the Court's questions of Edwin Benner's direct testimony in Docket number 24081 and 24082 may be written and taken as evidence in this case to save time. That is the preliminary questioning.

The Court: Very well.

(The portion of the transcript stipulated to above is quoted as follows):

Direct Examination

Q. (By Mr. Wild): What is your position, Mr. Benner?

A. I am Vice-president and Secretary of the Bishop Trust Company, Limited, and in charge of the trust department.

Q. How long have you been in charge of the trust department?

A. Since the spring of 1946. [81]

Q. Prior to that time what was your position?

(Testimony of Edwin Benner Jr.)

A. I was a trust officer of Bishop Trust Company.

Q. And for how long?

A. I joined the trust company in 1934, and I have been in the Trust department at all times.

Q. I take it that your active business life, so far as your own participation is concerned since 1931 has been with Bishop Trust Company, Limited? A. That's right.

Q. What was the Bishop Trust Company's capital in 1940 and 1941, if you recollect?

A. It was approximately $1,200,000 with a surplus of a like amount.

Q. And what type of business did it conduct at that time?

A. It conducted a trust company business here in the Territory. Banks do not do trust business and trust companies do not do banking business, and so during that entire time it was operated strictly as a professional fiduciary, with side issues such as insurance, real estate sales and brokerage, but its main business is administration of estates, trusts, guardianships, agency accounts, acting as corporate trustee of all sorts and types, transfer agents, that type of business.

Q. In one fiduciary capacity or another do you have as part of your duties the management of various types of properties? A. Yes, indeed.

Q. You might explain that.

A. The normal trust or estate that we handle, of course, consists primarily of stocks and bonds

(Testimony of Edwin Benner Jr.)

or ownerships in real estate, but very often we have the problem of the administration of proprietorships or own the control or total outstanding shares of businesses, and these change year for year as the estates are probated and closed out. Some of our trusts have operated business for many years, though. I can give you a few examples.

Q. I wish you would give me some examples of business that you have operated in a fiduciary capacity.

A. We have just closed up an estate that has as its principal asset the controlling interest in a small structural steel company here in town with business operating right straight along. Our officer in charge was necessarily right on the job sometimes in the office, and so forth. We do own the controlling interest, through one of our fiduciary accounts, the largest specialty store, McInerny, Limited, that does $3,000,000 of business each year. I personally am secretary-treasurer of that company and sign all checks, incidentally. I receive daily statements of its sales volume by department all the way through. We have a very active part. [83]

Another business we are handling right now is the Honolulu Tile Business owned by the Worthington Estate. When Mr. Worthington passed away —it was his own business, and it was necessary that we step in and operate it, and not being familiar with that business we had some difficulty for several months and lost money until we were able to get things organized properly with an efficient man-

(Testimony of Edwin Benner Jr.)

ager, and are now pulling it out of the red and are doing very well. Our men in charge of that particular estate consult with me every week about their problems that they have there. They are on the job right along too.

We have handled dairies; we have handled ranches; we have handled ice cream business. In 1944 and 1945 we administered the estate of Frances Wadsworth on the island of Maui. Mrs. Wadsworth at the time of her death was owner of the Maui Soda and Ice Works. That business owned the Coca-Cola franchise on the island of Maui. I made 18 trips to Maui during the year 1945 in connection with that business, taking a very active part in it.

The Court: Is that as executor?

The Witness: We were temporary administrators to start with, the license was issued in our name at first, and then to us as executor.

The Court: And what do you do there, try to liquidate the company as quickly as possible? [84]

The Witness: We operated it just about a year. In 1944 and 1945 were boom years here in the islands because of the tremendous number of service people here, and bottling companies and business of that nature did a tremendous business, and rather than a liquidation program we continued to operate so that we would have a going business to sell to someone. We negotiated a sale eventually to a man who had been the West Coast agent for Coca-Cola. He

(Testimony of Edwin Benner Jr.)

was able to secure the consent of the Coca-Cola Company.

Mr. Nyquist: Objection, your Honor. I don't think there is any occasion to go into other bottling company cases.

The Court: We don't need to go any further on that——

Q. (By Mr. Wild): What other type of business?

A. I just jotted down a few, auto sales——

The Court: I think that is enough.

The Witness: We have the Ford agency in Hilo right now that we are administrating."

(End of stipulated portion of transcript.)

Q. (By Mr. Wild): Mr. Benner, when did you first become acquainted with the problems of the Thomas Brodhead partnership and trust?

A. About the time that the partnership and the trust were created. I was a co-signer with Mr. White on the Thomas Brodhead trust on behalf of the Bishop Trust Company, co-trustee. [85]

Q. Now during the operations of the special partnership, so long as the Thomas Brodhead trust was a special partner, did you have consultations, or were you present at consultations with Mr. Brodhead about the business?

A. It is very possible I did, although that trust was a co-partner for a very short time, Mr. Wild, and I can't specifically answer yes to that question.

Q. Now you were aware of the change, the settlement, for instance, of the Elizabeth Brodhead trust

(Testimony of Edwin Benner Jr.)
and the change in the partnership so that the Elizabeth Brodhead trust acquired a one-half interest as special partner, in the Thomas Brodhead Company, a partnership?

A. Yes, I discussed that.

Q. Now after that period of time did you have conferences and receive information from Thomas Brodhead concerning the Elizabeth Brodhead trust investment in the special partnership?

A. Yes, concerning partnership affairs I did at times.

Q. Were you given accounts from time to time periodically?

A. Yes, we were given annual audits and statements, and then Mr. Brodhead at times would come over with pencilled memoranda to discuss. Those discussions, when he brought over a pencilled memorandum showing the financial condition and the need to borrow funds. I think the bank was the Bank of Hawaii that he used or was using in the partnership, [86] and those are the only written statements that I saw. He never left a written memorandum about finances, the particular picture at that moment. It was just memorandum form. I had many other discussions with him and Mr. White at the same time on leaving the money in the business because of the growing pains that the business was suffering, although my conversations with him initially were on the more limited side, as Mr. White was in charge of the account and I just sat in or pinch hit for him while he was away. I later took

(Testimony of Edwin Benner Jr.)

charge of the account entirely. I think that was some time in 1946, in the summer of 1946.

Q. Was Mr. Mortimer Glueck a co-trustee with Bishop Trust? A. Yes.

Q. Under both trusts? A. That's right.

Q. Did Mr. Mortimer Glueck participate in one or more conversations with yourself and Mr. Brodhead concerning the affairs of the special partnership?

A. I recall several joint conversations with Mr. Glueck and Mr. Brodhead and myself at my desk, and others when we were sitting at Mr. White's desk where all four of us were present. Mr. Glueck's office for a great deal of this period of time was on the third floor of our building, and it was very handy for him to step downstairs to be with us.

Q. Did Mr. Thomas Brodhead attempt to dominate the investment policies of the trustees under the Thomas Brodhead trust?

A. No, he didn't. He did, as he stated on the stand a few moments ago, he made a request that we keep part of the funds in government bonds, and there was no objection to that because that is generally our policy in any type of trusts, and the other case was his suggestion that we purchase for the account of the Thomas Brodhead trust some sixty-odd shares of the Knight Newspaper. I have the name here. I would like to read it into the record, Knight's Newspapers, Incorporated. The value involved was almost $25,000. The corpus of the trust at that time, including investment income, was about

(Testimony of Edwin Benner Jr.)

$78,000. I didn't turn Mr. Brodhead down right off though, but I think he wasn't very encouraged when he made the suggestion, and it was referred to our investment research department for examination. Through the American Trust Company they contacted the Northern Trust Company at Chicago who gave us a report on this company.

Q. As a result of all that, did you accede to his request?

A. No, we very definitely turned it down as an unsound type, or undesirable type of investment trust.

Q. Now, Mr. Benner, during the period of time that the Thomas Brodhead trust was set up, at that time or thereabouts when the trust became a special partner in the partnership, was Bishop Trust Company named in any fiduciary capacity in [88] Mr. Brodhead's will?

A. We received a sealed envelope——

Mr. Nyquist: Objection, your Honor. The contents of Mr. Brodhead's will is a matter for the best evidence rule. It can best be proved by producing the will, and is not a subject for oral testimony.

Mr. Wild: If it is on the ground of the best evidence rule he is objecting, I haven't got it here, your Honor.

The Court: Sustained.

Q. (By Mr. Wild): Were you approached by Mr. Brodhead or by the trust company to ascer-

(Testimony of Edwin Benner Jr.)

tain whether they would be receptive to being named as executor in his will?

A. I have no personal knowledge.

Mr. Wild: No further examination.

The Court: Any questions?

Mr. Nyquist: Yes, your Honor.

Cross Examination

Q. (By Mr. Nyquist): Mr. Benner, you have given some testimony on direct examination about investments made by each of these trusts and about the consulting with the settlors about the investments. Did you, for example, in making an investment for the Thomas Brodhead trust, would you always secure the approval of Mr. Brodhead before making an investment?

A. Well, of course, the original investment was indicated [89] in the trust instrument. Then the sale of that investment, that interest to the Elizabeth Brodhead trust, he was aware of and approved. Then I think our first investment was in— Well, I would answer yes to your question.

Q. And on the Elizabeth Brodhead trust did you discuss with Mr. Brodhead the investments of that trust?

A. No, he didn't have anything to do with it.

Q. Did Mrs. Brodhead signify her approval on any of those investments before they were made?

A. Yes. We have only had two investment problems there. That was the investment of the $40,000 of surplus income that was in Brodhead Company

(Testimony of Edwin Benner Jr.)

in which we formed the corporation, the Brodhead Company, Limited, and then later a distribution from Ace Distributors to the trust, and we went through our formality of selecting and recommending, and she acquiesced.

Q. You have testified concerning conferences that you have had with Mr. Brodhead and possibly with the co-trustee concerning the conduct of the business. Did those conversations run primarily toward the financing or the financial end of the business operations?

A. Primarily so, in the taking on of new lines and things of that sort. I mean why he wanted to expand and why it was essential. Mr. Brodhead, frankly, felt he had a business that was really almost beyond him to handle because of the [90] tremendous increase in volume, and he was nervous about its administration and came in to talk with us. I think he was in our office very frequently. By that I mean every few weeks.

Q. Did you usually have to make specific requests to Mr. Brodhead to secure payments from the partnership which might be needed for the conduct of the trust operations?

A. That's right. When we needed funds we would phone him or write him a note, and he would distribute as requested.

Q. During the conduct of the operations of the business as a partnership, during that period of time did you generally have to make requests for such payments?

(Testimony of Edwin Benner Jr.)

A. Yes; to be frank, Mr. Brodhead was too engrossed in other things to think of paying any money over to us without asking for it.

Q. Was that one of these things you discussed in these financial discussions with him?

A. No, I don't think we had any discussions as to making him pay. We are fairly automatic in our requests. His coming in to discuss things with us did not concern non-payment of the funds.

Q. Did you ever tell or advise Mr. Brodhead how much salary he should draw from the business?

A. No, I was always aware of it. I think Mr. White was too. We discussed it. [91]

Q. But the decision was made by the general partner? A. That's right.

Q. Were you consulted about the creation of the Elizabeth Brodhead trust?

A. Not personally by Mrs. Brodhead or by Mr. Cades or Mr. Glueck. I discussed it with Mr. White in our office after apparently he had been approached, and we discussed the problem that had developed through this tax decision, and the best way that it would be worked out and of the proposal made. Where the proposal came from, I personally don't know.

Q. Do you know at the time the Elizabeth Brodhead trust was created whether $10,000 in cash was paid to the trustee?

A. From my examination of our records this morning, it appeared to me that no check was tendered. From our records it was apparently set up

(Testimony of Edwin Benner Jr.)
by a journal entry. I found that journal, as a matter of fact, and saw it. There was an indication of cash, but I think that was just to show that that tied in with the trust instrument to get the detailed books set up, but I don't think we actually ever received a check for it.

Q. And after the Thomas Brodhead trust had made the sale of its interest to the Elizabeth Brodhead trust, can you tell us what it received in the way of consideration, what form the consideration took? [92]

A. Well, it was part of this same series of journal entries, the one I referred to just now, the $40,000 investment that the Thomas Brodhead trust had had in the partnership, as a result of these journal entries they became these two things. They became a note of $30,000 from the Elizabeth Brodhead trust and a $10,000 note from the Thomas Brodhead company, the partnership. That was the $40,000 of assets we carried on our books then as a result of that, and the partnership interest disappeared as an asset of the Thomas Brodhead trust.

Q. Did you consider that these notes receivable that the Thomas Brodhead trust received had value substantially equal to the partnership interest which it sold?

A. We were satisfied on what transactions took place from our examination and discussion.

Q. But my question specifically is did you consider the interest in the going business of the Thomas Brodhead partnership equal in value to one $10,000

(Testimony of Edwin Benner Jr.)

note of the partnership and the other $30,000 note of the trust whose only asset was an interest in the partnership?

A. Yes, not any more than that, though.

Q. How much income did you anticipate receiving from these notes receivable?

A. It was stated in the notes. I have forgotten the amount, but materially less, maybe three or four per cent. [93]

Q. Three or four per cent of the total of $40,000?

A. Yes.

Q. Which would be about how much?

A. I think 3% of $40,000 is $1,200 a year.

Q. And do you recall how much income——

Mr. Wild: Isn't that note in the record? It is stipulated. I think it is 5%.

Q. (By Mr. Nyquist): Assuming it to be 5% and the interest on $40,000 being $2,000, was that substantially less than the income the trust had received from the partnership during the preceding year? A. Yes.

Q. Do you recall approximately how much the income was?

A. We hadn't operated an entire year, as I recall, and we received, I think the record will show, $38,000 or something like that. I think that is about the amount.

Q. And you consider an investment that produces $38,000 in part of a year as being substantially the equivalent in value of an investment that will produce $2,000 in a full year?

(Testimony of Edwin Benner Jr.)

A. I might answer that yes and no. We have a lot in this picture.

Q. There are a lot of qualifications to that, I suppose. Would you like to offer an explanation?

A. I would, because I wouldn't want you to think a trust company just drops good assets. We were confronted with a [94] problem, very frankly, from our standpoint and our discussion in the office, of losing completely an interest in a partnership that we were holding for the benefit of certain minor children, or the alternative of selling that partnership interest to another entity which was being formed by still another party for the benefit of these same minor children, and we thought that it was the best interest, without any qualification, to go ahead with the plan as it was worked out.

Q. Then you would not have agreed to such a plan if the beneficiaries had not been identical in the two trusts, is that true? A. That is true.

Q. You spoke about one investment that was suggested by Mr. Brodhead, I believe Knight Newspaper, and upon investigation you decided that it was not an advisable investment. A. Yes.

Q. Did you then discuss the matter further with Mr. Brodhead? A. I told him of our decision.

Q. Did he agree with that decision?

A. He accepted it.

Mr. Nyquist: That's all, your Honor.

The Court: Is that all? [95]

Mr. Wild: That's all.

The Court: Just step down.

(The witness was excused.)

Mr. Wild: Petitioners rest, your Honor.

Mr. Nyquist: Respondent rests, your Honor.

The Court: What about the time for filing briefs in this case? Will it vary a little bit from the last?

Mr. Cades: May we have seventy days for the opening and forty-five and forty-five?

The Court: Mr. Clerk, will you give them the dates?

The Clerk: Petitioners' brief will be due August 29, Respondent's answering brief October 15, and Petitioners' reply November 29.

The Court: Those will be the dates. We will close the record in this case.

(Whereupon, at 12:40 p.m. on Wednesday, June 20, 1951, the hearing was concluded, and an adjournment was taken to 2:00 o'clock p.m., the same date.) [96]

Wednesday, June 27, 1951

Mr. Cades: If your Honor please, may we ask that the Brodhead cases be reopened for the submission of two or three more exhibits which counsel agree should be made a part of the record?

The Court: Very well.

Mr. Cades: We would like to offer in evidence a photostatic copy of the income tax return of Thomas Brodhead for the year 1947.

Mr. Nyquist: No objection.

The Court: It will be received.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 46.)

Mr. Cades: We would also like to offer in evidence the tax return of Elizabeth S. Brodhead for the year 1947.

Mr. Nyquist: No objection, your Honor.

The Court: It will be received.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 47.)

The Court: Anything further?

Mr. Cades: That's all, your Honor.

Mr. Nyquist: Nothing further.

The Court: If there is nothing further, we will adjourn sine die.

(Adjournment sine die.)

[Endorsed]: T.C.U.S. Filed July 18, 1951.

[Endorsed]: No. 13805. United States Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. Thomas H. Brodhead and Elizabeth S. Brodhead, Respondents. Transcript of the Record. Petition to Review Decisions of the Tax Court of the United States.

Filed April 13, 1953.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 13805

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD, Respondents.

PETITIONER'S DESIGNATION OF RECORD

The petitioner hereby designates for inclusion in the printed record on appeal the following portions of the typewritten record received by this Court from the Clerk of the Tax Court of the United States in the above-entitled cause:

1. Docket Entries, No. 29,391.
2. Docket Entries, No. 29,392.
3. Petition (with exhibit), No. 29,391.
4. Answer, No. 29,391.
5. Petition (with exhibit), No. 29,392.
6. Answer, No. 29,392.
7. Amendment to Answer, No. 29,392.
8. Reply to Amendment to Answer, No. 29,392.
9. Stipulation of Facts, with Exhibits 1 through 10 and 18 through 24.
10. Transcript of Proceedings, 6-20-51 and 6-27-51, pp. 1, 22 through 97.

11. Findings of Fact and Opinion.
12. Decision, No. 29,391.
13. Decision, No. 29,392.
14. Petition for Review, Nos. 29,391 and 29,392.
15. Statement of Points, Nos. 29,391 and 29,392.
16. This Designation.

Dated: April 28, 1953.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
Attorney for Petitioner.

[Endorsed]: Filed April 30, 1953. Paul P. O'Brien, Clerk.

No. 13,805

In the United States Court of Appeals for the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE, PETITIONER,

v.

THOMAS H. BRODHEAD AND ELIZABETH S. BRODHEAD, RESPONDENTS.

ON PETITION FOR REVIEW OF THE DECISIONS OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE PETITIONER

H. BRIAN HOLLAND,
Assistant Attorney General.

ELLIS N. SLACK,
LEE A. JACKSON,
JOSEPH F. GOETTEN,
Special Assistants to the Attorney General.

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In the United States Court of Appeals for the Ninth Circuit

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COMMISSIONER OF INTERNAL REVENUE, PETITIONER,

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ON PETITION FOR REVIEW OF THE DECISIONS OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE PETITIONER

OPINION BELOW

The opinion of the Tax Court (R. 140-161) is reported at 18 T. C. 726.

JURISDICTION

The petition for review in these cases involves deficiencies aggregating $169,553.49 in the federal income taxes of the taxpayer, Thomas H. Brodhead, and his wife, Elizabeth S. Brodhead, for the years 1943, 1944, 1945 and 1948. (R. 5, 18, 163-169.)

On February 7, 1950,[1] the Commissioner of Internal Revenue mailed to the taxpayer and his wife notices of deficiencies in their income taxes for the years in question. (R. 11, 29.) Within 150 days thereafter, on July 3, 1950 (R. 1, 4), the taxpayer and his wife, pursuant to Section 272 of the Internal Revenue Code, filed petitions with the Tax Court for redetermination of such deficiencies. The proceedings were consolidated for hearing in the court below. (R. 2, 4.) On October 31, 1952, decisions of the Tax Court were entered redetermining the deficiencies. (R. 162, 163.) On January 19, 1953, the Commissioner filed his petition for review invoking the jurisdiction of this Court under Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948. (R. 163-167.)

QUESTIONS PRESENTED

1. Whether in transferring property in trust for the benefit of his minor children then living and those yet to be born the taxpayer retained sufficient control over that property to be treated for tax purposes as the recipient of income therefrom when (a) the trusts were required to use that property to acquire a special or limited partner's interest in a family partnership in which the taxpayer was the controlling general partner, and (b) the trusts were not free to terminate or transfer their interest once the partnership was created.

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[1] There were added to the gross income of the taxpayer and his wife for each of the years in question amounts in excess of 25 per cent of the amounts of gross income stated in their joint returns. (R. 13, 33, 36, 38.) See Section 275(c) of the Internal Revenue Code. On or about January 18, 1949, a consent was executed extending to June 30, 1950, the period within which an income tax might be assessed or a deficiency notice mailed to the taxpayer for the year 1943. (R. 151-152.)

2. Whether trusts, which the taxpayer claims should be recognized for tax purposes as special or limited partners solely on the basis of their contribution of gift capital to the partnership, were the true owner-contributors of such capital when they were not free to withhold such capital from the partnership, to transfer the partnership interest allegedly required for the capital, or to withdraw from the partnership either the capital or income attributable to it.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and Regulations are set forth in the Appendix, *infra*.

STATEMENT

The facts found by the Tax Court, which are based in part upon a stipulation (R. 44-137), may be summarized as follows:

The taxpayer, Thomas H. Brodhead, and his wife, Elizabeth S. Brodhead, at all times material to these proceedings were residents of the Territory of Hawaii. They have three children born December 29, 1939, November 19, 1942, and May 1, 1945. (R. 141.)

In and prior to 1942 the taxpayer was engaged as an individual in operating a wholesale merchandise business in Honolulu. The merchandise handled consisted of a great variety of articles which were sold to post exchanges and ships' service stores and included drug items, razor blades, dungarees, shoes, underwear, work shirts, shower clogs, pocket knives, candy, gum and miscellaneous items. (R. 141.)

The taxpayer came from a family of short-lived people on his father's side and he was quite concerned about the length of his own life. Conditions in Hawaii in 1942

were not conducive to a feeling of long life. He was determined to make some provision for his children so that they would have a better education than he had. In September 1942 the taxpayer and his wife had one child, and were expecting the birth of another. The taxpayer's business grew rapidly after the start of World War II, and he wanted some means of having it carried on for the benefit of his children in the event of his death. Also, because of the size to which the business had grown in 1942 he felt that he needed someone to help him with it. (R. 141-142.)

Mortimer J. Glueck had been a personal and business acquaintance of the taxpayer for a number of years, had kept his books on a part time basis, and had advised him generally. Glueck had a commission business, and in 1942 he was getting too busy with it to be able to assist the taxpayer and advised him to get other assistance. Glueck and the taxpayer had many discussions as to what provision the latter should make for his children. (R. 142.)

Bishop Trust Company, in and prior to 1942 conducted a trust company business in the Territory of Hawaii. It is operated as a professional fiduciary, with side issues such as insurance, real estate sales, and brokerage. Its main business is the administration of estates, trusts, guardianships and agency accounts. The normal trust or estate handled by the trust company consists of securities or interests in real estate. However, it has at times administered proprietorships and the controlling shares of incorporated businesses. In the administration of such properties it has operated various businesses including a structural steel mill, a department

store, dairies, ranches, a bottling company, and an automobile agency. (R. 142.)

In 1942 Glueck and the taxpayer sought the advice of counsel, and it was agreed that a trust should be created for the benefit of the children of the taxpayer and his wife and that the trust should become a partner with the taxpayer in his business. The taxpayer asked Glueck to be one of the trustees so that with his knowledge of the business he could carry it on in the event of the taxpayer's death. The taxpayer also wanted Bishop Trust Company as a trustee for the general assistance and advice that it could give. (R. 143.)

On September 30, 1942, the taxpayer created the Thomas H. Brodhead Trust, naming Mortimer J. Glueck and Bishop Trust Company as trustees. Corpus of the trust was stated to be $40,000. It consisted of a one-half interest in the taxpayer's business which at that time had a net worth of $80,000. Under the trust agreement, the $40,000 corpus was to be contributed to the capital of a special partnership to be organized concurrently for a 50 per cent interest therein. (R. 143.)

The trustees were required to accumulate all trust income during the continuance of the trust, but they had discretion to pay out net income for the maintenance, support, and education of the children of the settlor, or if income was insufficient they could use corpus. All income not used for such purposes was to be accumulated and added to corpus. The trustees were authorized to pay to any child of the settlor any time after attaining age 21, as they deemed proper, such portion of corpus and accumulated income as constituted one share, such share to be determined by considering the trust estate

to be divided into as many equal shares as there should be children then surviving or lineal descendants of any deceased child. (R. 143-144.)

The trust was to continue until 20 years after the death of the settlor. The trust property and accumulated income were then to be distributed to the surviving children of the settlor (other than those to whom the distribution of a share may have previously been made) and the issue of any deceased children. If there were no children or issue then surviving, distribution was to be made to those persons, other than the settlor, who would be the heirs-at-law of the last survivor of the children of the settlor. (R. 144.)

The trustees could terminate the trust at any time after the termination of the special partnership, in which event distribution was to be made to the settlor's children and issue of any deceased children. (R. 144.)

The trustees were given broad powers to invest and reinvest and manage the trust property, but during the life of the settlor they were required to obtain his consent to all investments. After the settlor's death the trustees were to be restricted in making investments to those which trustees are permitted by law to make. However, they could in any event make advances or loans to the special partnership without liability for any loss resulting therefrom. (R. 144.)

The settlor reserved the right to transfer additional property to the trust. The trustees were required to furnish annual statements of account to the benficiaries. The corporate trustee was given the custody of all money or securities in the trust. (R. 144-145.)

The trust was declared to be irrevocable by the settlor. It was provided that in no event should any of the trust

property or income be paid to or inure to the benefit of the settlor. (R. 145.)

Any alteration, amendment, cancellation, or revocation of any provisions of the trust required the written consent of the trustees and all of the beneficiaries. (R. 145.)

A special partnership was formed by a document dated as of September 30, 1942. The taxpayer was referred to therein and signed the agreement as "General Partner." The trustees of the above described trust are referred to and signed as "Special Partner." The partnership adopted the name of T. H. Brodhead Company. Its purpose was to acquire the assets and carry on the business theretofore conducted by the taxpayer. Other purposes are stated including the carrying on of any business that may lawfully be carried on by a partnership. (R. 145.)

The initial capital of the partnership was $80,000 which was the book value of the net assets that it acquired. It was agreed that $40,000 was the capital contribution of each of the partners and that each had a 50 per cent interest. (R. 145.)

The general partner who was actively engaged in the business was to receive compensation for his services which was to be charged as an expense in computing partnership profits. The remaining profit, or loss, was to be divided in proportion to the capital contributions. Profits attributable to each partner's interest could be withdrawn from time to time as the partners deemed advisable. (R. 145-146.)

The trustees had all the powers, rights, and duties of a special partner as prescribed by designated sections of the Special Partnership Law of the Territory of

Hawaii, and were not liable for partnership debts beyond the extent prescribed by law. (R. 146.)

Only the general partner had authority to transact the business of the partnership, or incur obligations. He was to establish the policy of the partnership. The special partner could at all times investigate the partnership affairs and advise the general partner as to its management. (R. 146.)

The general partner could not assign or mortgage any part of his interest. The special partner could assign its interest with the consent of the general partner. (R. 146.)

Proper partnership books and records were to be kept and each partner was to have full access to them. The books were to be audited at least once a year, and a copy of the auditor's report was to be delivered to each partner. Annual accounts were to be taken, showing the capital of the partnership and the interest of each partner therein and copies were to be furnished to each partner. (R. 146.)

The partnership could be terminated by the general partner on two months' written notice. On termination, debts were to be paid, and any balance remaining was to be applied first to advance accounts of the partners, then to capital, then between the partners in the manner provided for division of profits. If the balance after payment of debts was insufficient to pay in full the advance accounts of all partners, the special partner was to be paid first. (R. 146-147.)

In the event of the death of the general partner, his representative had the option of succeeding to or carrying on his interest in the business as a general partner. (R. 147.)

The partnership was to continue for a ten-year period and thereafter from year to year until terminated by either partner giving three months' notice. (R. 147.)

By bill of sale dated as of the close of business on September 30, 1942, the taxpayer conveyed to the special partnership the rights, property, assets, and privileges owned by him and used in his merchandising business. The partnership agreed in the bill of sale to assume the liabilities disclosed by the balance sheet attached thereto. The balance sheet listed assets in the amount of $178,598.73, current liabilities in the amount of $98,598.73, and capital in the amount of $80,000. Among the assets listed were cash, $21,532.34; accounts receivable, $64,667,35; and merchandise inventory, $27,310.44. (R. 147.)

The required documents concerning the organization of the special partnership were duly filed and publication was made in a Honolulu paper. (R. 147.)

Early in 1943, the taxpayer was advised by his attorney that under a recent court decision he might be subject to federal income tax on all of the income of the Thomas H. Brodhead trust without being able to get any of the trust income to use to pay the tax. In that situation, it was possible that he might have been unable to pay the tax. He was advised by counsel that a new trust could be created, omitting the features that might make the income of the first trust taxable to him, to acquire the interest of the first trust in the partnership. (R. 147-148.)

Following discussions among the taxpayer and his wife, the trustees of the Thomas H. Brodhead trust, and counsel, the taxpayer's wife Elizabeth S. Brodhead on February 28, 1943, created the Elizabeth S. Brodhead trust. The trustees of that trust were the same as

those of Thomas H. Brodhead trust. At that time, the taxpayer gave his wife $10,000 which she paid in to the trust created by her. Both the taxpayer and his wife filed federal gift tax returns in which they reported the gifts of $10,000 made by them. (R. 148.)

The provisions of the Elizabeth S. Brodhead trust were substantially the same as those of the Thomas H. Brodhead trust. The principal differences were that the wife's trust did not give discretion to the trustees to distribute income for maintenance, support, or education of the beneficiaries during minority, and it was to terminate when the youngest child attained the age of 33 years. (R. 148.)

On February 28, 1943, the Elizabeth S. Brodhead trust purchased from the Thomas H. Brodhead trust its 50 per cent interest in the special partnership. That interest was duly assigned to the Elizabeth S. Brodhead trust by an instrument dated February 28, 1943, in which the taxpayer, as general partner gave his consent to the assignment. The Elizabeth S. Brodhead trust paid the Thomas H. Brodhead trust the sum of $10,000, and gave its note for the unpaid balance of the purchase price of the 50 per cent interest in the amount of $30,000 with interest at five per cent. Interest was paid periodically, and the principal of the note was paid off by payments made in 1945 and 1949. The legally required certificate of change of the special partnership and affidavits were duly filed, and notice was duly published. (R. 148-149.)

An independent firm of auditors was employed by the partnership to make audits of the partnership business and to prepare annual statements. (R. 149.)

The taxpayer received compensation for his services to the partnership for the periods and in the amounts as follows (R. 149):

Period or Year	*Amount*
October 1, 1942, to February 28, 1943..	$ 6,250.00
Fiscal year ended February 28, 1944..	15,000.00
Fiscal year ended February 28, 1945..	18,000.00
Fiscal year ended February 28, 1946..	18,000.00
Fiscal year ended February 28, 1947..	18,000.00

As of the close of business on February 28, 1947, the name of the special partnership was changed from T. H. Brodhead Company to Ace Distributors. The instrument changing the name was executed by the taxpayer as general partner and by Mortimer J. Glueck and Bishop Trust Company, trustees under the Elizabeth S. Brodhead trust, as special partner. The necessary documents to effect the change were duly filed and publication was duly made. (R. 149-150.)

As of the close of business on February 28, 1947, the partnership, under its new name of Ace Distributors, assigned T. H. Brodhead Company, a Hawaiian corporation, certain rights, property and assets used in its business, subject to balance sheet liabilities, which properties had a net book value of $80,000. In payment therefor the corporation issued 4,000 shares of its stock to the general partner and an equal number to the special partner. The necessary documents in connection with the organization of the corporation and the issuance of its stock were duly filed. (R. 150.)

During the period of operations of the special partnership, the general partner discussed the problems of the business frequently with the trustees of the two trusts. Whenever a financial report on the business

was issued he furnished copies to the trustees. The general partner conferred with the corporate trustee as to investment of the funds of the first trust. In one instance it accepted his suggestion as to an investment and in another instance it refused to do so. He discussed with the trustees possible means of financing an expansion of the partnership business which in the war years was increasing in volume. (R. 150.)

The partnership T. H. Brodhead Company filed partnership returns on an accrual and fiscal year basis ending on the 28th of February. Its first return on that basis was filed for the fiscal year ended February 28, 1943. Returns were filed on that basis for each of the subsequent fiscal years 1944 through 1949. (R. 150-151.)

The Thomas H. Brodhead trust and the Elizabeth S. Brodhead trust filed federal fiduciary returns each year and duly paid the tax shown to be due thereon. None of the funds of the trusts has ever been paid out to the beneficiaries thereof. Out of the income of the trusts there have been paid the expenses of each, such as trustee fees, tax service fees, and the federal and territorial income taxes. (R. 151.)

On September 30, 1950, the assets of the Thomas H. Brodhead trust amounted to a total of $86,918.97, which consisted of cash in the amount of $2,109.48 and investments in stocks, bonds, and savings and loan certificates with a cost of $84,809.49. (R. 151.)

On February 28, 1951, the assets of the Elizabeth S. Brodhead trust amounted to a total of $85,673.03, which was made up of cash, $3,858.90; partnership equity in Ace Distributors, $2,904.85; accounts receivable received in partial liquidation of Ace Distributors, $17,-

000; 4,000 shares of stock in T. H. Brodhead Company, $40,000; other stocks having a cost of $13,409.28; savings and loan certificates with a cost of $8,500. (R. 151.)

The two trusts were bona fide trusts for the benefit of the children of the settlors, and the taxpayer and his wife had no substantial control over, or interest in, the corpus or income thereof. (R. 152.)

The taxpayer and the trustees of the Thomas H. Brodhead trust and of the Elizabeth S. Brodhead trust really and truly intended to, and did, join together for the purpose of carrying on the business of T. H. Brodhead Company and sharing in its profits and losses. (R. 152.)

STATEMENT OF POINTS TO BE URGED

The points upon which the Commissioner relies as the basis for this proceeding are set forth at pages 167-169 of the record. In substance, they are that the Tax Court clearly erred in holding that the taxpayer did not retain sufficient control over the property which he had purportedly given away to remain taxable on the income attributable to that property and in holding that the donee-trusts were the true owner-contributors of the gift capital upon which their claims of partnership status were based.

SUMMARY OF ARGUMENT

In the case at bar we have an almost identical factual pattern to that in *Commissioner* v. *Sultan,* No. 13,804, now pending in this Court, and to that in *Toor* v. *Westover,* where this Court held that the taxpayer in that case remained the substantial owner of the assigned property. The trustees here were not free to remain out of the partnership; they were not free to terminate the

partnership or transfer their interest as special or limited partner; the donor, as controlling general partner, retained the powers of management and control over the time and amounts of distributions of profits. The Tax Court erred, therefore, in holding that in transferring property in trust for the benefit of his minor children the taxpayer did not retain sufficient control over the property to be treated for tax purposes as the recipient of income therefrom.

To have acquired partnership status for tax purposes an alleged partner must have contributed to the partnership one or both of the ingredients of income—capital or services. Where partnership status is based solely on the contribution of gift capital, the alleged partner must have been the true owner-contributor of that capital. As a special or limited partner the trust in the case at bar could not have contributed services to the conduct of the partnership business. Moreover, it was not the owner-contributor of the gift capital because it was not free to withhold such capital from the partnership, to transfer its interest in the partnership, or to withdraw either the gift capital or the income attributable to it. The Tax Court erred, therefore, in holding that the trust was entitled to recognition as a partner for tax purposes.

ARGUMENT

I

The Tax Court Erred in Holding that in Transferring Property In Trust for the Benefit of His Minor Children the Taxpayer Did Not Retain Sufficient Control Over that Property To Be Treated for Tax Purposes as the Recipient of Income Therefrom

The case at bar presents a factual pattern almost identical to that in *Toor* v. *Westover,* 200 F. 2d 713

(C.A. 9th), certiorari denied, 345 U.S. 975, and likewise almost identical to that in *Commissioner* v. *Sultan,* No. 13,804, presently pending before this Court.[2] In our brief in the *Sultan* case, we have discussed at some length this Court's decision in the *Toor* case and other applicable decisions, and have pointed out why those decisions require a reversal of the Tax Court. For like reasons, a reversal is required in the present case.

As in the *Toor* and *Sultan* cases, this case involves a package arrangement of trusts and a special or limited partnership. In this case, as in *Sultan,* the Tax Court, failing to focus on the end result of the partnership-trust arrangement, has improperly treated each separately and has ignored or viewed as immaterial critical facts found by it. In this manner, we submit, the Tax Court has reached a clearly erroneous conclusion, as it did in *Sultan.*

Like the donee in the *Toor* case, *supra,* the donee in the present case "was neither free to remain out of the partnership nor free to terminate or transfer his interest once the partnership was created." The donee-trust was not free to remain out of the partnership because of paragraph lettered (a) of each of the two trust indentures. Paragraph lettered (a) of the Thomas H. Brodhead trust indenture provided that the trustees should use the entire amount transferred to them by the settlor to purchase a 50 per cent interest in the partnership and that they should continue to be a special or limited partner. (R. 53.) Paragraph lettered (a) of the Elizabeth S. Brodhead trust indenture provided that

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[2] In *Commissioner* v. *Eaton,* No. 13,806, docketed in this Court immediately following the instant case, the same factual pattern is also presented.

the trustees should use the entire amount transferred to them by the settlor to purchase the interest of the Thomas H. Brodhead Trust in the partnership and that they should continue to be a special or limited partner.[3] (R. 93.) The donee-trust was not free to terminate the partnership during its ten-year term [4] because of paragraph numbered 11 of the special partnership agreement. Paragraph numbered 11 provided that the partnership could be determined or terminated by the general partner, namely, the taxpayer alone. (R. 72.) The donee-trust was not free to transfer its interest in the partnership because of paragraph numbered 8 of the special partnership agreement. Paragraph numbered 8 provided that the special or limited partner (the donee-trust) could assign its share or interest in the partnership only with the consent of the general partner (the taxpayer) who had full power and discretion to give or withhold such consent. (R. 71.) Moreover, paragraph numbered 7 of the special partnership agreement provided that only the general partner (the taxpayer) would have authority to transact partnership business and that he would establish the policy of the partnership (R. 70); paragraph numbered 4 provided that only such portion of the profits attributable

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[3] The taxpayer's wife, Elizabeth S. Brodhead, clearly acted merely as a conduit for his transfer of the corpus to the Elizabeth S. Brodhead trust. Having this second trust created to acquire the interest of the first trust was necessary to eliminate those provisions of the first trust believed to render the trust income taxable to the taxpayer-settlor because those provisions appeared in paragraph lettered (c) of the first trust indenture which by virtue of paragraph lettered (o) could not be amended. (R. 54, 62.) Court approval of the trust company's being a co-trustee in the arrangement was not necessary because such approval had been previously obtained under almost identical circumstances. See *Commissioner* v. *Sultan,* No. 13,804, now pending on appeal to this Court.

[4] The term of the partnership in the *Toor* case was 13 years.

to a partner's interest could be withdrawn from the partnership as the partners (including the taxpayer) might deem advisable [5] (R. 69). Thus, the assignor in the case at bar, as in the *Toor* case,[6] remained the substantial owner of the partnership interest which he purportedly had given away.

In *Helvering* v. *Horst,* 311 U.S. 112, the Supreme Court stated (p. 119):

> We have held without deviation that where the donor retains control of the trust property the income is taxable to him although paid to the donee.

In the case at bar the trustees did not acquire the usual attributes of ownership with respect to the trust property. They were required to invest it in the partnership; as a limited partner, they had no voice in the use of their investment; and they were not free either to withdraw or transfer their interest. The taxpayer-settlor, on the other hand, retained complete control over the trust property which he had purportedly given away. He was assured that it would immediately be returned for use in the business which he controlled. The partnership which he dominated could also use it in any other business. Its use by the partnership was to be without restriction by the donee-trust—because the

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[5] Paragraph numbered 4 provided that the amount of distributive net profits would be arrived at after deducting the compensation of the general partner actively engaged in the business in such amount as the partners from time to time agreed upon constituting the reasonable value of the services rendered. (R. 69.)

[6] In the *Toor* case the trustee-bank apparently acted completely in a fiduciary capacity. In the instant case, however, paragraph lettered (l) of the first trust indenture and paragraph lettered (k) of the second trust indenture provided that the trustees would not be answerable or accountable for any loss or damage resulting from any act consented to by the settlor. (R. 61, 100.)

donee-trust was only a special or limited partner. Its continued availability was assured because the donee-trust was not free to withdraw or transfer its interest. Determinations of the taxpayer, as general partner, were binding upon the partnership and he established the policy of the partnership. By his purported transfer of property in trust for the benefit of his minor children, therefore, the taxpayer in reality merely parted with the right to receive income from that property.[7] Of course, as observed in our *Sultan* brief and as stated by the Supreme Court in *Commissioner v. Sunnen,* 333 U. S. 591, 604:

> It has long been established that the mere assignment of the right to receive income is not enough to insulate the assignor from income tax liability.

II

The Tax Court Erred in Failing To Hold That Neither Trust Was Actually the Owner-Contributor of the Capital Necessary To Give It Recognition as a Special or Limited Partner for Tax Purposes

In our brief in the *Sultan* case, we have pointed out that in *Commissioner* v. *Culbertson,* 337 U.S. 733, the

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[7] The taxpayer also even retained the right indefinitely to use that income since by virtue of paragraph numbered 4 of the special partnership agreement the maximum to which the trust was actually entitled was an account receivable. (R. 69.) Use of trust property income already paid to the trustees was also made possible by the provision of paragraphs lettered (g) and (f) of the first and second trust indentures, respectively, that the trustees could make loans to the partnership without liability for any resulting losses. (R. 57, 96-97.) See Section 29.22(a)-21(e)(2) of Treasury Regulations 111, Appendix, *infra.* Further control by the taxpayer-settlor of the trust property income was contained in the provision of these same paragraphs that approval of the taxpayer-settlor was required for all investments of such income by the trustees. (R. 57, 96.) This provision alone would be sufficient to render the trust property income for 1948 taxable to the taxpayer-settlor under Section 29.22(a)-21(e)(4) of Treasury Regulations 111, Appendix, *infra.*

Supreme Court held that in order to acquire partnership status for tax purposes, it is necessary not only that the alleged partner have contributed either services or capital to the partnership [8] but also that, where such status is claimed on the basis of a contribution of gift capital, the alleged partner have been the true owner of that capital.

In the case at bar the taxpayer and his wife have not contended that either trust, as a special or limited partner, did, or could under the laws of Hawaii, contribute services to the conduct of the partnership business. The partnership status of each trust, therefore, must rest upon the claim that it was the true owner, and therefore the contributor, of the gift capital. Of course, an alleged partner may be the true owner-contributor of gift capital if he voluntarily puts such capital in or voluntarily leaves it in the partnership. Here, however, as previously mentioned, each donee-trust had no option. It was not free to remain out of the partnership nor free to terminate or transfer its interest once the partnership was created. The gift of capital to each trust was conditioned upon the investment of that capital in the partnership. At the will of the general partner, the taxpayer, such capital, and also the income attributable to it, was to remain available for partnership use, a use with respect to which each trust, as a special or limited partner, had no voice. Under the circumstances, neither trust was the true owner of the gift capital. Accord-

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[8] The opinion of the court below has placed unwarranted emphasis on the matter of intent in the instant case as it did in the *Sultan* case; and it may be observed here as there that while the intent of the parties is frequently the ultimate question in determining whether a family partnership arrangement is genuine, of course, parties do not become partners merely by intending to be such.

ingly, neither trust was entitled to recognition as a partner for tax purposes.

CONCLUSION

The decisions of the Tax Court are erroneous and should be reversed.

Respectfully submitted,

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AUGUST, 1953.

APPENDIX

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U.S.C. 1946 ed., Sec. 22.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

(26 U.S.C. 1946 ed., Sec. 182.)

Revised Laws of Hawaii (1935):

CHAPTER 225. PARTNERSHIPS, REGISTRATION OF.

* * * * *

SEC. 6870. *Between individuals.*—A partnership may be formed between two or more individuals for the transaction of any lawful business. A special

partnership may be formed between one or more persons, called general partners, and one or more persons called special partners, for the transaction of any business.

* * * * *

SEC. 6880. *Only general partners act.*—The general partners only shall have authority to transact the business of a special partnership.

SEC. 6881. *Special partners may advise.*—A special partner may at all times investigate the partnership affairs and advise his partners or their agents as to their management.

SEC. 6882. *May loan money. Insolvency.*—A special partner may lend money to the partnership or advance money for it, or to it, and take from it security therefor, and as to such secured loans or advances has the same rights as any other creditor, but in case of the insolvency of the partnership all other claim which he may have against it must be postponed until all other creditors are satisfied.

SEC. 6883. *Receive interest and profits.*—A special partner may receive such lawful interest and such proportion of profits as may be agreed upon, if not paid out of the capital invested in the partnership by him or some other special partner, and is not bound to refund the same to meet subsequent losses.

SEC. 6884. *May not withdraw capital.*—No special partner, under any pretense, may withdraw any part of the capital invested by him in the partnership during its continuance.

SEC. 6885. *Result of withdrawing capital.*—If a special partner withdraws capital from the firm, contrary to the provisions of sections 6883 or 6884, he thereby becomes a general partner.

Treasury Regulations 111, promulgated under the Internal Revenue Code:

> SEC. 29.22(a)-21 [as added by T. D. 5488, 1946-1 Cum. Bull. 19, and as amended by T. D. 5567, 1947-2 Cum. Bull. 9.]. *Trust income taxable to the grantor as substantial owner thereof.*—
>
> * * * * *
>
> (e) *Administrative control.*—Income of a trust, whatever its duration, is taxable to the grantor where, under the terms of the trust or the circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust. Administrative control is exercisable primarily for the benefit of the grantor where—
>
> * * * * *
>
> (2) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor to borrow the corpus or income, directly or indirectly, without adequate interest in any case, or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions; or
>
> * * * * *
>
> (4) any one of the following powers of administration over the trust corpus or income is exercisable in a nonfiduciary capacity by the grantor, or any person not having a substantial adverse interest in its exercise, or both: a power to vote or direct

the voting of stock or other securities, a power to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments, and a power to reacquire the trust corpus by substituting other property of an equivalent value.

* * * * *

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No. 13,805

IN THE

United States Court of Appeals

For the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

THOMAS H. BRODHEAD and ELIZABETH S. BRODHEAD,
Respondents.

On Petition for Review of the Decisions of the Tax Court of the United States.

BRIEF FOR RESPONDENTS.

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No. 13,805

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BRIEF FOR RESPONDENTS.

OPINION BELOW.

The opinion of the Tax Court (R. 140-161) is reported at 18 TC 726.

JURISDICTION.

The petition for review in these cases involves deficiencies aggregating $169,553.49 in the federal income taxes of the taxpayer, Thomas H. Brodhead (herein called the "Taxpayer"), and his wife, Eliza-

beth S. Brodhead, for the years 1943, 1944, 1945 and 1948 (R. 5, 18, 163-169).

On February 7, 1950[1] the Commissioner of Internal Revenue (herein called the "Commissioner") mailed to the Taxpayer and his wife notices of deficiencies in their income taxes for the years in question (R. 11, 29). Within 150 days thereafter, on July 3, 1950 (R. 1, 4), the Taxpayer and his wife, pursuant to Section 272 of the Internal Revenue Code, filed petitions with the Tax Court for redetermination of such deficiencies. The proceedings were consolidated for hearing in the court below (R. 2, 4). On October 31, 1952, decisions of the Tax Court were entered redetermining the deficiencies (R. 162, 163). On January 19, 1953, the Commissioner filed his petition for review invoking the jurisdiction of this court under Section 1141(a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948 (R. 163-167).

QUESTIONS PRESENTED.

1. Whether on all of the evidence in the record the Tax Court's finding of fact, that Thomas H. Brodhead and the trustees of the Thomas H. Brod-

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[1]There were added to the gross income of the Taxpayer and his wife for each of the years in question amounts in excess of 25 per cent of the amounts of gross income stated in their joint returns (R. 13, 33, 36, 38). See Section 275(c) of the Internal Revenue Code. On or about January 18, 1949, a consent was executed extending to June 30, 1950, the period within which an income tax might be assessed or a deficiency notice mailed to the Taxpayer for the year 1943 (R. 151-152).

head Trust and of the Elizabeth S. Brodhead Trust really and truly intended to, and did, join together for the purpose of carrying on the business of T. H. Brodhead Co. and sharing in its profits and losses, is so unreasonable as to require a reversal of the decision below.

2. Whether the Tax Court erred in holding that in the creation of the two trusts, the Taxpayer and his wife did not retain sufficient interest in or control over the corpus or income thereof to render the Taxpayer liable for income taxes on the income thereof.

STATUTES AND REGULATIONS INVOLVED.

The pertinent statutes and regulations are set forth in the Appendix, *infra.*

STATEMENT.

The Taxpayer does not controvert the Commissioner's statement of the case in the Brief for the Petitioner (herein cited "Brief") (pp. 3-13).

SUMMARY OF ARGUMENT.

The Commissioner does not deny that under the local law the Thomas H. Brodhead Trust and the Elizabeth S. Brodhead Trust were valid and binding trusts, and the special partnership was a valid and

subsisting special partnership. The sole question presented is whether the special partnership should be recognized and given effect under the revenue laws of the United States. The test for determining that question has been formulated by the Supreme Court of the United States in *Commissioner v. Culbertson,* 337 U.S. 733, 93 L.ed 1659 (1949), and whether any given partnership measures up to that test is a question of fact. *Commissioner v. Culbertson, supra,* at 741-42. A finding of fact made by the Tax Court will not be disturbed on review unless it is clearly unreasonable. *Boehm v. Commissioner of Int. Rev.,* 326 U.S. 287, 293-94, 90 L.ed 78, 84-85 (1945); *Commissioner of Int. Rev. v. Scottish Am. Inv. Co.,* 323 U.S. 119, 123-24, 89 L.ed 113, 116-17 (1944); *Helvering v. Kehoe,* 309 U.S. 277, 279, 84 L.ed 751, 753 (1940). An examination of the record in the case at bar reveals not merely a substantial basis therein for the Tax Court's finding on this question, but clear and convincing evidence virtually compelling the conclusion at which the Tax Court arrived.

The income of a private express inter vivos trust, although not payable to the grantor thereof, may be taxed to him under the revenue laws of the United States if the grantor retains a sufficient "bundle of rights" in the trust, *Helvering v. Clifford,* 309 U.S. 331, 84 L.ed 788 (1940), as where a grantor creates a short term trust, names himself as trustee, grants himself broad discretion as to the income to be distributed and retains a reversionary interest in the corpus of the trust. In the case at bar, however, the

Taxpayer made an absolute irrevocable transfer in trust to independent trustees, for a substantial term, had no control over the income of the trust, and possessed no reversion in the corpus thereof. Under the special partnership agreement the Taxpayer had no control over the corpus or income of the trust which he could exercise for his own benefit. The case of *Helvering v. Clifford, supra,* is clearly inapplicable to the instant case.

The Commissioner in his argument (Brief 14-18) reads into the opinion of this court in *Toor v. Westover,* 200 F.2d 713 (1952), a departure from the test laid down by the Supreme Court in *Commissioner v. Culbertson, supra,* and seeks to establish a rule of law making the issue in family partnership cases one to be determined by the very kind of "objective test" so clearly repudiated by the Supreme Court in *Commissioner v. Culbertson.*

ARGUMENT.

I.

THE EVIDENCE APPEARING IN THE RECORD CLEARLY SUPPORTS THE TAX COURT'S FINDING OF FACT, THAT THE TAXPAYER AND THE TRUSTEES OF THE THOMAS H. BRODHEAD TRUST AND OF THE ELIZABETH S. BRODHEAD TRUST REALLY AND TRULY INTENDED TO, AND DID, JOIN TOGETHER FOR THE PURPOSE OF CARRYING ON THE BUSINESS OF THOMAS H. BRODHEAD CO. AND SHARING IN ITS PROFITS AND LOSSES.

The Commissioner does not deny that under the local law the Thomas H. Brodhead Trust and the Elizabeth S. Brodhead Trust were valid and binding

trusts, and the special partnership was a valid and subsisting special partnership. The sole question presented is whether the special partnership should be recognized and given effect under the revenue laws of the United States. The test for determining that question has been formulated by the Supreme Court, in *Commissioner v. Culbertson, supra,* in the following language:

> ". . . whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise. . . ." (337 U.S. 733 at 742-43)

> ". . . if the donee of property who then invests it in the family partnership exercises dominion and control over that property—and through that control influences the conduct of the partnership and the disposition of its income—he may well be a true partner. Whether he is free to, and does, enjoy the fruits of the partnership is strongly indicative of the reality of his participation in the enterprise. . . ." (*id.* at 747)

A review of the record reveals ample support in the evidence for the Tax Court's finding on the question as posed in the *Culbertson* case.

A. *The Agreement.* The terms of the special partnership agreement (R. 65-79) clearly reflect the intent of the parties to join as partners in the enterprise. The first (unnumbered) paragraph of the agreement (R. 65-66) recites that the parties "do hereby form with each other a special partnership for the purpose of acquiring and thereafter conducting the business heretofore carried on by Thomas Holmes Brodhead . . . and for other purposes . . . .", which other purposes are spelled out in detail in paragraph 1 of the agreement (R. 66-67).

Paragraph 3 of the agreement (R. 68) sets forth the respective capital contributions of the partners and secures to the special partner all of the powers, rights and duties of special partners as prescribed by Chapter 225 of the Revised Laws of Hawaii 1935 (See Appendix, *infra*) as the same might from time to time be amended. The same paragraph provides that the special partner shall not be liable for the debts of the partnership beyond the limits set by Section 6887 of the Revised Laws of Hawaii 1935 (See Appendix, *infra*), as the same might from time to time be amended.

Paragraph 4 of the agreement provides for compensation for services rendered to the partnership by the general partner, in such amount as the partners, including the special partner, might agree upon, and provides that such compensation shall be chargeable as an expense of the business for the purposes of computing the net profits of the partnership (R.

68-69). The same paragraph provides for annual division of the net profits of the partnership in proportion to the respective capital interests of the partners, and permits either partner to withdraw such portion of his share of profits as both partners may from time to time deem advisable (R. 69).

Paragraph 7 of the agreement expressly recognizes the right of the special partner to investigate the partnership affairs and to advise the general partner as to its management at all times (R. 70).

Paragraph 9 of the agreement requires that proper partnership books of account be kept, and expressly confers upon each of the partners the right at all times to have full and free access to, and to make copies of, the partnership books (R. 71).

Paragraph 10 of the agreement requires annual general accounts to be taken of all of the assets and liabilities and dealings and transactions of the partnership, and expressly requires that copies of such accounts be sent to each partner (R. 71).

Although pursuant to paragraph 8 of the agreement the general partner could not assign or mortgage his share of or interest in the partnership or its assets or profits at any time, the special partner was free to assign its interest in the partnership with the consent of the general partner (R. 71).

Paragraph 11 of the agreement provides that upon the determination of the partnership from whatever cause, the assets of the partnership remaining after

payment of its debts and expenses shall be applied first to the payment of the amounts standing to the partners' credit in their advance accounts, and then to repayment of their capital contributions, according the special partner priority in distribution in each case (R. 72-73).

B. *The Conduct of the Parties.* The evidence in the record concerning the conduct of the parties in pursuance of the partnership agreement clearly reflects that they intended to, and did, join together for the purpose of carrying on the enterprise and sharing in its profits and losses.

The taxpayer rendered services to the partnership as its manager, in accordance with paragraph 5 of the agreement (R. 182, 219). For those services he was paid reasonable compensation, which was deducted as an expense of the partnership business in computing the profits thereof (R. 182-83).

The special partner investigated the partnership affairs and advised the Taxpayer, as general partner, as to its management in accordance with the partnership agreement and with the applicable law. In this connection the evidence shows that the Taxpayer consulted very frequently with the special partner, every day or every couple of days; furnished it all financial statements; and took up and discussed with the special partner such matters as financing, the need for added capital, and the taking on of new lines (R. 185-86, 219, 229-31, 234-35).

The testimony of the trust officer who succeeded to the responsibility for the trusts' accounts shows that the special partner consulted and advised with the Taxpayer as to how business was going, the need of retaining capital in the business due to its continuous growth, taking on new lines, and the amount of the Taxpayer's salary as general manager (R. 229-31, 234-35). Audit reports, and oral reports on operations, were furnished to the special partner regularly (R. 185, 230).

With the exception of certain periods when, with the consent of the special partner, certain partnership profits were retained in the business to permit the accumulation of additional capital, the special partner insisted upon, and received, its full distributive share of the partnership income (R. 131, 133, 134, 200-01, 234-35).

When the Elizabeth S. Brodhead Trust purchased the interest of the Thomas H. Brodhead Trust in the special partnership, the Thomas H. Brodhead Trust received the full fair value of its interest as the purchase price (R. 193), and when the assets of the partnership were sold, the consideration paid therefor was divided between the Taxpayer and the special partner in strict accordance with their respective interests in the partnership enterprise (R. 160-84).

The parties to the special partnership agreement, including the trusts, held themselves out to the public as general and special partners respectively, by filing

in the office of the Treasurer of the Territory of Hawaii a duly executed certificate of special partnership, by publishing a statement of substance of certificate of special partnership in the Honolulu Advertiser on four different days (R. 46, 85-92), by subsequently filing an appropriate certificate of change of special partnership and publishing a statement of substance thereof in the Honolulu Advertiser on four different days (R. 47-48, 108-15), and thereafter by filing a further certificate of change of special partnership and publishing a statement of substance thereof in the Honolulu Advertiser on four different days (R. 48-49, 119-21).

C. *The Relationship of the Parties.* The evidence in the record with respect to the relationship of the parties lends ample support to the Tax Court's finding. Mortimer J. Glueck, co-trustee with Bishop Trust Company, Limited, of each of the trusts, had known the Taxpayer for many years and had grown up with Taxpayer's business as an advisor to the Taxpayer (R. 173-74, 176-77, 186-88, 216-17). There is no indication in the record that Mr. Glueck was in any way subservient to the Taxpayer in matters of business judgment. If anything, he appears to have been the dominant, independent party to their association (R. 174, 218-25).

Bishop Trust Company, Limited, had no prior relationship to the taxpayer, except that it was named executor in his will (R. 202), and it maintained at all times a relationship of independent arm's-length deal-

ing with him. The trust company exercised its independent judgment in deciding whether to become co-trustee and special partner (R. 221-22). Mr. Glueck and the trust company, as special partner, insisted upon full withdrawal of its share of the partnership earnings (R. 187, 191, 208, 249, 256-57), and exercised independent judgment on partnership affairs, including the sale of the partnership interest (R. 185, 199-200, 207-08, 215, 219-21, 231-32, 233, 238). In the matter of trust investments it exercised wholly independent judgment, even flatly refusing to make an investment suggested by the Taxpayer (R. 202-03).

D. *Abilities and Contributions of the Parties.* An examination of the evidence in the record relating to the respective abilities and contributions of the parties indicates ample support for the finding made by the Tax Court.

The Taxpayer had been in business since 1935, but in the years immediately preceding the formation of the special partnership the business had grown so large that he no longer felt capable of administering it alone (R. 172-75, 188-89, 216-18). He contributed both capital (R. 68) and services (R. 182, 219) to the enterprise.

Mortimer J. Glueck, co-trustee with Bishop Trust Company, Limited, of each of the trusts, had grown up with Taxpayer's business, and had long advised the Taxpayer in matters of business management. He was the successful proprietor of a business of his own. (R. 173-74, 176-77, 186-88, 216-17.)

Bishop Trust Company, Limited, conducted a trust company business in the Territory of Hawaii and had enjoyed wide experience in operating business enterprises in a fiduciary capacity. Among the various businesses operated by the trust company were included a structural steel company, a department store, a tile business, dairies, ranches, an ice cream business, a soda and ice works which held the Coca-Cola franchise for one of the Hawaiian Islands, and an auto sales agency (R. 226-29). Mr. Glueck and the trust company, as special partner, contributed capital to the enterprise (R. 90) and contributed advice and consultation to the full extent permitted by law (R. 185-86, 219, 229-31, 234-35).

Capital was an important income-producing factor in the partnership business. The business volume had increased tremendously as a result of the outbreak of World War II and the demands of the Armed Forces (R. 188-89), and throughout the existence of the special partnership, the special partner was concerned with the need for additional capital in connection with the expansion of the business (R. 230, 234).

E. *Actual Control of Income.* The evidence of record with respect to the exercise of actual control over the special partnership income fully supports the Tax Court's finding. The determination as to the time and amount of distributions of partnership earnings was required to be made by both partners jointly (R. 69) and the special partner firmly insisted upon

withdrawing the entire amount of its distributive share of the special partnership net profits (R. 201, 131, 133, 134). The special partner received and held under its exclusive dominion and control its entire distributive share of partnership income and none thereof was ever paid to the Taxypayer or used in discharge of his obligation to support his wife and children (R. 183).

F. *Business Purpose.* The evidence clearly reveals a proper business purpose for the formation of the partnership. The business represented the Taxpayer's entire worldly fortune, and it had grown to the point where he no longer felt able to carry it on by himself. Moreover, he was concerned over the possibility that his life expectancy was considerably shorter than normal. He desired to assure the continuity of the business irrespective of his early demise and to assure the availability of experienced management advisors. (R. 174-77, 188, 217-18.)

The purpose of preserving and continuing a going business as a family enterprise for the members of a family is a proper, legitimate, and indeed a commendable, business purpose. *Ardolina v. Commissioner of Internal Revenue,* 186 F. 2d 176 (3d Cir. 1951); *Nicholas v. Davis,* 204 F. 2d 200 (10th Cir. 1953).

There is no evidence in the record indicating any motive of tax avoidance or desire to reallocate income within the family group.

G. *Dominion and Control of Special Partner's Interest.* The Thomas H. Brodhead Trust was the donee of $40,000 (R. 52-53) and the owner thereof by virtue of a completed gift, as is more fully demonstrated under Point II, infra, which discussion is herein incorporated. And the Thomas H. Brodhead Trust invested the property given to it in the special partnership (R. 65-84). The Elizabeth S. Brodhead Trust was the donee of $10,000 (R. 92-107) and the owner thereof by virtue of a completed gift, as is also more fully demonstrated under Point II, infra, which discussion is herein incorporated. The Elizabeth S. Brodhead Trust purchased from the Thomas H. Brodhead Trust all of the latter's interest in the special partnership, thus in effect investing the property given to it in that partnership. To the extent that the differences between the two trusts are irrelevant here, the following discussion treats them as a single trust.

The Trust, as donee of the property which it had invested in the special partnership as a special partner, was clothed with all of the dominion and control permissible in a special partner under the law of the Territory of Hawaii (R. 68) and by its exercise of such dominion and control, it influenced the conduct of the partnership to the full extent that a special partner lawfully could do so (R. 185-86, 219, 229-31, 234-35). It had joint control over the disposition of special partnership income, and insisted upon full payment of all of the distributive share of special

partnership income allocable to it under the terms of the special partnership agreement (R. 131, 133, 134, 200-01, 234-35). The record clearly indicates that the special partner enjoyed the "fruits of the partnership" to the very fullest.

From the foregoing review of the evidence appearing of record in the case at bar, it is obvious that there is more than sufficient support for the Tax Court's finding of fact that the Taxpayer and the trustees of the Thomas H. Brodhead Trust and of the Elizabeth S. Brodhead Trust really and truly intended to and did join together for the purpose of carrying on the business of T. H. Brodhead Co., and sharing in its profits and losses.

II.

THE INCOME OF THE TRUSTS IS NOT TAXABLE TO THE TAXPAYER UNDER THE DOCTRINE OF HELVERING v. CLIFFORD OR THE COMMISSIONER'S REGULATIONS RELATING THERETO.

In *Helvering v. Clifford, supra,* settlor created a trust for a term of five years (with the proviso that it would terminate earlier on the death of either settlor or his wife) with himself as trustee and his wife as income beneficiary. On the termination of the trust the entire corpus was to revert to the settlor, while accrued or undistributed net income and net proceeds from the investment of any such net income was to be treated as his wife's absolute property. During the continuance of the trust, settlor was to pay

over such part of the income therefrom as he in his absolute discretion might determine, and during that period he had full power to exercise all voting rights incident to the trusteed shares of stock, to sell, encumber or otherwise dispose of any part of the corpus or income on such terms as he in his absolute discretion deemed fitting, and to invest any of the property of the trust by loans, secured or unsecured, by deposits in banks, or otherwise, without restriction as to the speculative character or rate of return of any such investment, or of any laws pertaining to the investment of trust funds. The Supreme Court, holding the settlor taxable on the income of the trust, in addition to the family relationship of the settlor and the beneficiary, emphasized the following factors: The short term of the trust, the fact that settlor was also the trustee, the absolute discretion in the settlor-trustee as to income to be distributed, and the reversion to the settlor upon the termination of the trust.

Underlying the decision of the Supreme Court in the *Clifford* case is the principle that where a purported donor retains controls over the subject matter of his gift, exercisable for his own personal benefit, sufficient to afford him the economic use and benefit of the property to substantially the same extent as if he were the absolute owner thereof, then the donor should remain taxable upon the income of that property.

An examination of the trust deeds in the case at bar shows that with the exception of the close family relationship between the Taxpayer and the bene-

ficiaries, none of the factors considered in the *Clifford* case is present here.

The Thomas H. Brodhead Trust was to terminate twenty years after the death of the Taxpayer or sooner upon the death of the last survivor of the Taxpayer's children if at that time no lawful issue of such children were alive (R. 55-56). The Trustees, but not the Taxpayer, had power to terminate the trust at any time not more than one year after the trust might cease to be a member of the special partnership.

The Elizabeth S. Brodhead Trust was to continue until the youngest child of Elizabeth S. Brodhead, the Taxpayer's wife, attained the age of thirty-three years or would have attained that age had he or she survived. At the time of the creation of the trust, Elizabeth S. Brodhead had two children, the youngest of whom was less than one year old. Thus, the minimum term of this trust was thirty-two years (R. 94-95). The trustees, but not the Taxpayer or his wife, had power to terminate the trust at any time not more than one year after the trust might cease to be a member of the special partnership.

The Taxpayer did not name himself a trustee of the Thomas H. Brodhead Trust. Instead he carefully selected Mortimer J. Glueck and Bishop Trust Company, Limited, as trustees, in order to take advantage of their experience and knowledge (R. 174-75, 176-77). Moreover, he named one Edouard R. L. Doty as successor to Mr. Glueck, and provided that if Mr. Doty

should be or become unable to act or decline to act or resign and after the death of Mr. Doty prior to the termination of the trust, the trust company might select some person as co-trustee in the place and stead of Mr. Doty (R. 62).

For similar reasons, and without any direction on the part of the Taxpayer, Elizabeth S. Brodhead selected Mr. Glueck and Bishop Trust Company, Limited, as trustees of the Elizabeth S. Brodhead Trust and made similar provisions with respect to successor trustees (R. 101, 205-07).

Any suggestion that by reason of his business and social association with the Taxpayer Mr. Glueck as co-trustee would be or was under the domination of the Taxpayer loses its force by reason of the fact that under the trust deed and the applicable law, the concurrence of both trustees would be required on all decisions. 2 *Scott, Trusts,* Sec. 194 (1939).

Since the Taxpayer was not a trustee of either of the trusts, it is self-evident that he could not under the trust deeds control the distribution or other disposition of the income therefrom.

The Taxpayer had no reversionary or remainder interest in either of the trusts. Upon the termination of the Thomas H. Brodhead Trust, the trust property was payable to the Taxpayer's living children and the lawful issue of his children who had died or, if there were no children or issue then living, to the heirs at law (other than the Taxpayer) of the last survivor of his children. If the trust were terminated

by the trustee as a result of its withdrawal from the special partnership, the trust property was payable to the then living children of the Taxpayer and the lawful issue of such of them as were dead.

Upon the termination of the Elizabeth S. Brodhead Trust (whether by expiration of its term or by action of the trustees), the trust property was payable to the living children of Elizabeth S. Brodhead and the lawful issue of such of them as were then dead, or if there were no living children or issue, to the heirs at law (other than Elizabeth S. Brodhead and the Taxpayer) of the last survivor of the children of Elizabeth S. Brodhead.

Thus it is evident that none of the factors emphasized by the Supreme Court in the *Clifford* case and repeatedly re-emphasized by the lower courts is present in this case.

Treasury Regulations 111, Section 29.22(a)-21[2] (herein called the "Clifford Regulations"), embody the Commissioner's exegesis upon the doctrine of *Helvering v. Clifford, supra,* and is applicable only to taxable years beginning on and after January 1, 1946. The Commissioner, in his argument (Brief 18, n.7) suggests in passing that the 1946 income of the trusts might be taxable to the Taxpayer under either or both of Sections 29.22(a)-21(e)(2) and 29.22(a)-21(e)(4). Section 29.22(a)-21(e)(2) asserts the Commissioner's opinion that income of a trust, whatever

[2]TD 5488, 1946-1, Cum. Bull. 19;
TD 5567, 1947-2, Cum. Bull. 9.

its duration, is taxable to the grantor where, under the terms of the trust or the circumstances attendant upon its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust through a power exercisable by the grantor or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, which enables the grantor to borrow the corpus or income directly or indirectly without adequate interest in any case or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions. Section 29.22(a)-21(e)(4) states the Commissioner's similar opinion with respect to a power, exercisable by the grantor in a non-fiduciary capacity, to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments.

The Commissioner suggests here that the terms of the trusts permitting the trustees to make loans to the partnership without liability for any resulting losses and providing that during the life of the Taxpayer the trustees shall obtain the consent of the settlor to the making of investments other than investments which trustees are permitted by law to make (R. 57, 96-97), render the 1946 income of the trusts taxable to the Taxpayer by the force of the Clifford Regula-

tions. The Commissioner's error in this respect arises largely from the fact that, assuming as his major premise the result for which he contends, namely, that the special partnership was a mere sham not entitled to recognition for income tax purposes, the Commissioner reasons that the Taxpayer and the partnership were one and the same entity for all purposes.

Without conceding the validity of the Clifford Regulations, the Taxpayer contends that those regulations are inapplicable in the case at bar. The trustees' power to make loans to the special partnership is a far different thing from a power to make loans to the Taxpayer. Any such loan would be to the partnership and for the partnership's account and not to the Taxpayer personally or for his personal benefit. As a partner in the special partnership, the Taxpayer stood in a fiduciary relation to each of the other partners, including the special partner. The Supreme Court of the Territory of Hawaii has recently reaffirmed in the strongest terms the proposition that there is scarcely any relation in life which calls for more absolute good faith than the relationship of partners, and that the obligation is even greater in the case of a managing partner. *Watumull v. Ettinger,* Sup. Ct., T.H., (Jan. 3, 1952); see also *Toor v. Westover,* 200 F.2d 713, 715 (9th Cir. 1952).

Assuming that a loan had been made from the trust to the partnership (and the record reveals no such loan), the Taxpayer could only have diverted the proceeds of the loan to his personal use and benefit by a violation of his clear and unambiguous

duty as a partner, which violation would give rise to a cause of action in favor of the trust against the Taxpayer. *Watumull v. Ettinger, supra.* The proposition that the naked power to seize property in violation of law renders the holder of that power taxable on the income of that property has never been seriously advanced.

In his argument from the requirement of consent to non-legal investments, the Commissioner overlooks the fact that the very terms of the Clifford Regulations restrict their applicability to a power exercisable *in a non-fiduciary capacity.* Under the doctrine of the *Clifford* case, a mere power to direct or veto proposed investments not exercisable for the benefit of the grantor does not render the holder of the power taxable on the income of the trust property. *Cushman v. Commissioner of Internal Revenue,* 153 F.2d 510 (2d Cir. 1946); *Kohnstamm v. Pedrick,* 153 F. 2d 506 (2d Cir. 1945).

In *Cushman v. Commissioner of Internal Revenue, supra,* petitioner created an irrevocable trust for the benefit of his children, naming himself and his wife as co-trustees with a corporate successor trustee. The petitioner reserved to himself, as grantor, the power to control retention or sale of trust property and to direct investment or reinvestment of trust funds. The Commissioner determined that the trust income was taxable to the petitioner under the doctrine of *Helvering v. Clifford,* supra, and the Tax Court agreed. On appeal to the Circuit Court for the

Second Circuit, the decision of the Tax Court was reversed. In answer to the Commissioner's contention the court held that petitioner's reserved power to control retention or sale of trust property and to direct investment and reinvestment of trust funds did not suffice to bring the case within the doctrine of *Helvering v. Clifford,* since the powers so retained could not be used contrary to the best interests of the beneficiary of the trust. Judge Chase, writing for the court, pointed out that ordinarily such powers are held in a fiduciary capacity and their exercise is subject to the scrutiny of the courts.

Again, in *Kohnstamm v. Pedrick, supra,* an appeal from a judgment dismissing the complaint entered after trial upon stipulated facts in the District Court for the Southern District of New York, plaintiff had created a trust for the benefit of his wife and children and had reserved to himself, as grantor, the power, among others, to direct the sale of any part of the trust fund and substitute equivalent investment and to vote all shares of stock held by the trust. Judge Learned Hand, writing for the court, in reversing the decision below, held that the power to direct the sale of trust assets and substitute equivalent investments, even when coupled with the other powers reserved, did not bring the plaintiff within *Helvering v. Clifford* and make him the owner of the trust property for tax purposes. See also *William P. Anderson,* 8 TC 921 (1947), Acq. 1947-2 Cum. Bull. 1; *Arthur L. Blakeslee,* 7 TC 1171 (1946), Acq. 1947-1 Cum. Bull. 1; *David L. Loew,* 7 TC 363 (1946);

Ernst Huber, 6 TC 219 (1946), Acq. 1946-1 Cum. Bull. 3.

The very terms of the trust deed in the case at bar (R. 57) negative any inference that the power reserved by the Taxpayer to require his consent to the making of certain investments during his lifetime is reserved for the benefit of anyone other than the beneficiary of the trust. The trust deed confers upon the trustees power to invest in property, real or personal, insofar as in their judgment they shall deem such investments advisable, and recites that in making such investments, the trustees shall not be restricted to investments which are legal for trust funds. The proviso reserving the power to require the Taxpayer's consent follows immediately after this grant and clearly relates to the making of investments which are not legal for trust funds. In every instance during the life of the Taxpayer, proposed investments must be investments which, in the judgment of the trustees, are advisable for the trust—that is, investments which are in the best interests of the income beneficiary and remainderman under the trust.

Thus, even if the Clifford Regulations are valid and applicable, the Taxpayer is not taxable upon the trust income by the force of those regulations.

If the Clifford Regulations are applicable, a determination that the 1946 income of the trust is taxable to the Taxpayer by the force of the regulations must result in the conclusion that the regulations as applied are invalid. As has been demonstrated above,

the Taxpayer is not taxable upon the income of the trust under the doctrine of *Helvering v. Clifford* alone. If the Taxpayer is held taxable on the 1946 income of the trust without any change in the facts or in the applicable law, then the regulations are invalid for the reasons stated in *Commissioner of Internal Revenue v. Clark,* 202 F.2d 94 (7th Cir. 1953). In that case the taxpayers created irrevocable trusts for the term of five years subject to extension by the grantors. Thereafter and for good cause, the grantors extended the irrevocable term of the trusts for at least five additional years, all other provisions remaining unchanged. The Commissioner assessed the 1946 income of the trusts to the grantors on the theory that the terms of the trusts were of less than ten years' duration and hence the income thereof was taxable to the grantors under the Clifford Regulations. The Tax Court held that the 1946 income of the trusts was not taxable to the grantors under Section 22(a) of the Internal Revenue Code or under *Helvering v. Clifford, supra,* or under the Clifford Regulations. On appeal by the Commissioner, the Court of Appeals for the Seventh Circuit, affirming the decision of the Tax Court, held that the Clifford Regulations as applied in that case were unreasonable and arbitrary and therefore void. Chief Judge Major for the court pointed out that the regulations created a conclusive or irrebuttable presumption and thus stated a rule of substantive law. Hence, without any alteration in the trust indentures and without any change in the relation of any of the parties

thereto that which was not income taxable to the grantors in 1944 and 1945 became income taxable to the grantors in 1946 solely as a result of the promulgation of the Clifford Regulations. Referring to cases in which the Supreme Court struck down as violative of due process a state statute which provided, in effect, that gifts of a decedent's estate made within six years of his death were made in contemplation thereof[3] and a congressional enactment which created a conclusive presumption that gifts made within two years prior to the death of the donor were made in contemplation of death,[4] Chief Judge Major stated that it appears that even Congress would be without power to create the conclusive presumption which the Treasury had attempted to create in the Clifford Regulations, and that it was even more certain that an administrative agency is without authority to promulgate such a regulation.

Exactly the same situation would exist in the case at bar if the trust income were taxed to the Taxpayer by the force of the Clifford Regulations. There was no significant change in the provisions of the trust deed between the years preceding and the year 1946. The Clifford Regulations create a conclusive or irrebuttable presumption, a rule of substantive law, effective January 1, 1946, that the existence of a power in the grantor to borrow corpus or income or of a power in a non-fiduciary capacity to veto proposed invest-

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[3]*Schlesinger v. State of Wisconsin,* 270 U.S. 230, 70 L.ed 557 (1926).

[4]*Heiner v. Donnan,* 285 U.S. 312, 76 L.ed 772 (1932).

ments makes the income of a trust the income of the grantor thereof. For the reasons set forth in *Commissioner of Internal Revenue v. Clark, supra,* any such application of the Clifford Regulations to the case at bar would be arbitrary, unreasonable and void.

Thus, the terms of the trust and the circumstances of its creation demonstrate that the income thereof is not taxable to the Taxpayer under the doctrine of *Helvering v. Clifford* or the extension of that doctrine embodied in the Clifford Regulations.

A consideration of the terms of the trust and the circumstances of its creation, taken together with the terms of the special partnership agreement and the operations of the special partnership leads to a like conclusion. The term of the special partnership agreement was initially for the ten years from October 1, 1942, to September 30, 1952, and thereafter from year to year until terminated by either partner (R. 76-77). The term of the special partnership agreement, however, had no effect upon the term of the trust, and on termination of the partnership agreement, the Taxpayer could not receive any part of the special partner's share of capital or earnings. Indeed, the special partner was granted priority in distribution on termination (R. 71-73).

The Taxpayer was the general partner in the special partnership, but, as pointed out above (pp. 22-23), his powers as such were not and could not lawfully be exercised for his own personal benefit. Under the rule laid down by the Supreme Court

of the Territory of Hawaii in *Watumull v. Ettinger, supra,* the Taxpayer owed a duty of absolute good faith to the special partner. See also *Toor v. Westover, supra.* Nor could the Taxpayer, as general partner, cause the assets of the special partnership to be diverted to any personal business of the Taxpayer. True, the special partnership agreement permitted the partnership to enter into a broad field of activity, but any business carried on by the partnership would be for the benefit and account of the partnership and of both of the partners therein.

Under the special partnership agreement, the Taxpayer had no power over the income of the partnership exercisable for his own benefit. The amount of the Taxpayer's compensation for services rendered to the partnership was to be determined by both of the partners, and by the very terms of the agreement was limited to the reasonable value of the services rendered (R. 69). Had the Taxpayer attempted to cause himself to be paid a salary in excess of that agreed upon with the special partner or an unreasonable salary (and there is no evidence in the record of any such attempt), he would have violated both the terms of the agreement and his duty of absolute good faith to his special partner, and would have been held to account under the rule of *Watumull v. Ettinger, supra.*

Similarly, partners' withdrawals from the partnership of the profits attributable to their interests was subject to the joint control of the Taxpayer and the

special partner (R. 69). Any retention of partnership earnings could be accomplished only with the consent of the special partner, and would inure to the benefit of the partnership and both of the partners therein. Any attempt on the part of the Taxpayer (and the record indicates no such attempt) to withhold the earnings of the special partner would constitute a violation of the rule of *Watumull v. Ettinger, supra,* and render the Taxpayer accountable therefor.

Nor could the Taxpayer obtain control of the corpus of the trust for his own use or benefit. The Taxpayer, as the general partner, could terminate the special partnership at any time upon certain written notice (R. 72). In the event of such termination, however, the assets of the special partnership, after payment of its debts and expenses, were to be distributed to the partners and the special partner was afforded priority in this distribution (R. 72-73). The Taxpayer, as general partner, could use the assets of the partnership in the partnership business and share in the profits and losses thereof, but he could not, without violating his duty of absolute good faith to his partner, divert those assets to his own personal business or to any other business. *Watumull v. Ettinger, supra.* Similarly, the option granted to the Taxpayer's representative to succeed to or carry on the interest of the Taxpayer in the business in the event of the Taxpayer's death, would afford to the Taxpayer's estate no power to divert the partnership

assets to the benefit of the estate, and all of the acts of the Taxpayer's representative upon succession to the Taxpayer's interest in the partnership would be governed by the same duty of absolute good faith which governed the Taxpayer during his lifetime.

Thus it is clear that under the doctrine of the *Clifford* case, the trust deed and special partnership agreement taken together with the circumstances surrounding the same did not reserve to the Taxpayer any power sufficient to render him taxable upon the income of the trust or the special partner's distributive share of the partnership income.

It is clear from the Commissioner's argument (Brief, 14-18) that he asserts the income in question to be taxable to the Taxpayer solely under the doctrine of *Helvering v. Clifford, supra,* and relies almost exclusively upon the language of the opinion of this Court in *Toor v. Westover, supra.* The Commissioner's only challenge to the *bona fides* of the special partnership is based on his assertion that the trustees did not become the real owners of the trust property (Brief, 18-19), and if this contention fails, his entire argument falls.

The Commissioner maintains that the trustees ". . . did not acquire the usual attributes of ownership with respect to the trust property" (Brief, 17) and lists nine propositions in support of this contention. That these nine propositions, to the limited extent that they have a basis in the law or the record, do not

lead to the conclusion contended for, appears from the following *seriatim* examination thereof:

1. ". . . They were required to invest it in the partnership. . . ." (Brief, 17). The Commissioner's position here appears to be that a transfer of property in trust wherein the trustee is not granted the power of sale but is directed to retain the property so transferred cannot so shift the ownership of the property as to render the trustee or the trust beneficiaries taxable upon the income thereof. On this theory a transfer or gift of a partnership interest would never be effective to shift the incidence of taxation, since the donee would have no choice but to become a partner or refuse the gift. Simply to assert these propositions is to accomplish their refutation.

2. ". . . as a limited partner, they had no voice in the use of their investment . . . ." (Brief, 17). This statement simply is not borne out by the law, the special partnership agreement or the record. As pointed out above, the trustees were granted all of the voice in the use of their investment that it was possible to grant to a special partner under the law of the Territory of Hawaii and exercised their rights to the fullest. There is no doubt that a special or limited partner may be recognized under the revenue laws of the United States as a bona fide partner in a special or limited partnership. *Nicholas v. Davis,* 204 F. 2d 200 (10th Cir. 1953); *John A. Morris,* 13 TC 1020 (1949), Acq. 1950-1 Cum. Bull. 3; *Walter*

R. Stutz, 10 TCM 506 (1951); *William Collins, Sr.,* 7 TCM 830 (1948); *Jacques Spira,* 7 TCM 371 (1948).

3. ". . . they were not free either to withdraw or transfer their interest . . . ." (Brief, 17). This statement is not altogether free from its misleading elements, inasmuch as the special partner was not *absolutely* free to withdraw or transfer its interest, but was free to make such withdrawal or transfer with the consent of the general partner (R. 71). It may be noted that the general partner was not free to assign or mortgage his interest under any circumstances *(ibid.).* The Commissioner apparently concedes that restriction on the transferability of a partner's interest is not fatal to the existence of a bona fide partnership, for he cites with approval (Brief, 15) *Toor v. Westover, supra.* See also *Joseph Middlebrook, Jr.,* 13 TC 385 (1949), Acq. 1950-1 Cum. Bull. 3; *William Collins, Sr., supra.* Nothing in the language of the Supreme Court in *Helvering v. Clifford* would indicate that the donor of all or a part of a special partner's interest in a special partnership ipso facto retains powers over the subject matter of the gift sufficient to make him taxable upon the income thereof. Indeed, in *Nicholas v. Davis, supra,* the capital invested by the limited partners was given them by the general partners with the express understanding that such capital would be invested in the limited partnership; yet, the Court of Appeals for the Tenth Circuit held the partnership to be bona fide for tax purposes.

4. ". . . The taxpayer-settlor, on the other hand, retained complete control over the trust property which he had purportedly given away. . . ." (Brief, 17). Here again, the Commissioner confuses the Taxpayer and the special partnership. Far from retaining complete control over the trust property, the Taxpayer divested himself of all interest therein and of all control thereof excepting only such control as he could lawfully exercise in discharge of his duty of absolute good faith to his partner. *Watumull v. Ettinger, supra.* As has been pointed out, retained powers of control over trust property, if they are to render the income therefrom taxable to the donor, must be exercisable by the donor in a non-fiduciary capacity.

5. ". . . He [the Taxpayer] was assured that it would immediately be returned for use in the business which he controlled. . . ." (Brief, 17). Assurance that the trust corpus would be invested in a given business appears to be irrelevant under the Clifford doctrine unless that business is, in fact, controlled by the Taxpayer. And as has been so often repeated, the business was controlled by the Taxpayer only in his capacity as a fiduciary under a duty of absolute good faith to his fellow partner. Indeed, if this and the preceding proposition support the Commissioner's contention, then no transfer in trust wherein the donor named himself trustee could ever be sufficient to shift the incidence of taxation on the income of the transferred property, for in every such case the

donor, as donee-trustee, would retain full control of the property (subject, of course, to the terms of the trust instrument) in his fiduciary capacity as trustee.

6. ". . . The partnership which he [the Taxpayer] dominated could also use it in any other business. . . . " (Brief, 17). As has already been demonstrated, this statement is not in accord that the facts. The partnership was not "dominated" by the Taxpayer except as the general partner therein and, as such, the Taxpayer was bound to discharge a duty of absolute good faith to his fellow partner. Moreover, the partnership could not use the trust property "in any other business" except to the extent that the partnership engaged in another business. And if the partnership engaged in another business, it could do so only on behalf of and for the account of the respective partners, each of whom would share in the fruits of the enterprise in accordance with his capital contribution.

7. ". . . Its [the trust property's] use was to be without restriction by the donee-trust—because the donee-trust was only a special or limited partner. . . ." (Brief, 17-18). This statement merely recasts the statements numbered 2 and 4, *supra,* and is no more in accord with the facts or the law than are those statements.

8. ". . . Its [the trust property's] continued availability was assured because the donee-trust was not free to withdraw or transfer its interest. . . ." (Brief,

18). This statement is a mere repetition of the statement numbered 3, *supra.*

9. " . . . Determinations of the Taxpayer, as general partner, were binding upon the partnership and he established the policy of the partnership. . . ." (Brief, 18). This statement, too, is not without its misleading aspects, for only some, but not all, of the Taxpayer's determinations were binding on the partnership. Thus, as has been pointed out above, the determination as to Taxpayer's salary and as to the time and amount of withdrawal of earnings was to be made jointly by the Taxpayer and the special partner. Moreover, as has been repeatedly reiterated, any determination by the Taxpayer, as the general partner, could lawfully be made only in absolute good faith and in the interests and for the benefit of the partnership. No such determination could lawfully be made by the Taxpayer for his own personal benefit. It is far from uncommon for partnerships, general, special or limited, to utilize managing partners, and the practice has been given express recognition by the courts. *J. A. Riggs Tractor Co.,* 6 TC 889 (1946); *George Brothers & Co.,* 41 BTA 287 (1940).

Clearly, the powers held by the Taxpayer under the trust deed and partnership agreement—and he held very few, if any, of those attributed to him by the Commissioner—do not singly or in the aggregate constitute the "bundle of rights" requisite for the invocation of the doctrine of *Helvering v. Clifford.*

The Commissioner, in his reliance on *Toor v. Westover, supra,* seeks to narrow the holding of this court to a degree unwarranted by the facts and the opinion therein.

That case originated as an action in the District Court for the Southern District of California against a collector of internal revenue to recover sums paid as a result of deficiency assessments of income tax. The case was tried, argued and submitted, and the District Court made and entered its findings of fact. These findings revealed the following situation: Plaintiff made trust agreements with a bank for the benefit of his children, and the trustee of the trusts so created executed articles of limited partnership with plaintiff as the general partner. Under the trust agreements the trustee was restricted to investments either in businesses in which plaintiff was a partner or principal shareholder, or in government bonds. The trust agreements were revocable by the plaintiff as grantor. Plaintiff retained exclusive dominion of the property, the disposition and allocation of the funds derived from the partnership business and all matters requiring judgment or management.

In no instance did the bank use its independent judgment on partnership matters nor did it exercise any of the rights of partnership even by way of advice. The bank, as limited partner, did not exercise dominion and control over the trust corpus in the business nor did it influence the conduct of the partnership or the disposition of the income thereof. The

partnership articles conferred on the plaintiff the absolute right to purchase the interest of the limited partner at its book value. There was no business purpose underlying the creation of the partnership, and the District Court commented that the conclusion was warranted that its sole object was to diminish tax liability.

The District Court, applying the *Tower,*[5] *Lusthaus,*[6] and *Culbertson,*[7] rules found as a matter of fact that the plaintiff and the trustee-bank did not in good faith intend to join together in the present conduct of the business enterprise (94 F. Supp. 860, 864-66) and entered judgment for defendant.

On appeal to this court, the judgment of the District Court was affirmed in an opinion by Circuit Judge Orr. This court held that the donee trust did not become the substantial owner of a partnership interest which would entitle the partnership to recognition for tax purposes. In reaching that conclusion this court stated that considering the fact that the donee was neither free to remain out of the partnership nor free to terminate or transfer its interest once the partnership was created, and that the plaintiff, as general manager, retained the powers of management and full discretion as to time and amounts of distribution of profits, the plaintiff re-

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[5]*Commissioner of Int. Rev. v. Tower,* 327 U.S. 280, 90 L.ed 670 (1946).

[6]*Lusthaus v. Commissioner of Int. Rev.,* 327 U.S. 293, 90 L.ed 679 (1946).

[7]*Commissioner v. Culbertson, supra.*

mained the substantial owner of the interest he purported to have given away.

In its statement of the case this court recounted substantially all of the facts hereinabove referred to. It quoted the reports of the Senate and House Committees on the Revenue Bill of 1951[8] and in particular the statement that:

> "Substantial powers may be retained by the transferor as a managing partner or in any other fiduciary capacity which, when considered in the lights [sic] of all the circumstances, will not indicate any lack of true ownership in the transferee. In weighing the effect of a retention of any power upon the bona fides of a purported gift or sale, a power exercisable for the benefit of others must be distinguished from a power vested in the transferor for his own benefit."

saying of this statement:

> "We believe that this has always been the law". (200 F.2d 713, 716.)

Thus, it appears that in arriving at its decision in *Toor v. Westover, supra,* this court, while pointing out for the guidance of the lower court the significance of the fact that the donee-trust was neither free to remain out of the partnership nor to terminate or transfer its interest once the partnership was created, did not intend to rule that those facts alone and without regard to the other factors present—the revo-

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[8]Sen. Rep. No. 781, 82d Cong. 1st Sess. (1951); H.R. Rep. No. 586, 82d Cong. 1st Sess. (1951).

cability of the trust, the plaintiff's exclusive domination of the property and disposition of the funds derived from the partnership, the special partner's completely passive role, and the plaintiff's absolute right to buy out the limited partner at book value—among others—were sufficient in themselves to establish retained substantial ownership in the purported donor.

To adopt the reading of *Toor v. Westover, supra,* contended for by the Commissioner, is to impute to this Court a departure from the doctrine of both the *Culbertson* and the *Clifford* cases. The Supreme Court, in the *Culbertson* case, stressed the importance of considering all of the facts in any family partnership case, rather than attempting to apply one or two "objective" tests. And in the *Clifford* case, that Court emphasized the cumulative effect of the entire bundle of rights retained by the purported donor, and held that they amounted in the aggregate to substantial ownership.

The Commissioner, however, urges that the holding of this Court in the *Toor* case sets up two objective tests in family partnership cases, namely, that in order to be a bona fide partner, recognizable for income tax purposes, a partner must be (1) free to remain out of the partnership and (2) absolutely free to terminate or transfer his interest once the partnership is created. Not only does this reading of the *Toor* case depart from the rationale of the *Culbertson* and *Clifford* cases, but it also tends to bring this court

into unnecessary conflict with the Courts of Appeals for the Eighth and Tenth Circuits. *Thompson v. Riggs,* 175 F. 2d 81 (8th Cir. 1949); *Nicholas v. Davis,* 204 F. 2d 200 (10th Cir. 1953).

Thompson v. Riggs, supra, was an appeal from a judgment for the plaintiff in an action for refund of income taxes. The plaintiff was the owner of a 60% interest in a partnership in which the remaining 40% interest belonged to his son. Plaintiff transferred out of his 60% interest 5% each to six irrevocable trusts for the benefit of plaintiff's wife and plaintiff's son's family. Plaintiff, his son and a bank were named trustees of each of the trusts. Plaintiff, his son and the trustees then entered into a new partnership agreement.

The trust instruments provided in relevant part that on all matters concerning the management and control of the partnership business, authority to speak for the trustees was vested in plaintiff and his son to the exclusion of the bank, and that the bank was to act as a naked trustee exercising no discretion and being charged with no liability or responsibility for or arising out of the conduct of the partnership business. The trustees could withdraw from the partnership but any decision as to whether to do so was to be made solely by the plaintiff and his son to the exclusion of the bank. Similarly, the trustees could acquire additional interests in the partnership, but the right to determine whether to do so was vested solely in the plaintiff and his son. The partnership

agreement provided that the management of the partnership business was vested in the plaintiff and his son (and plaintiff's grandson when and if he attained maturity and so long as he retained an interest in the business either as trustee or individually), and further provided that in the event of any disagreement as to the management of the partnership business, the decision of the plaintiff would control so long as he retained an interest in the business individually or as trustee. No partner could assign his interest (except to another partner) without the consent of all of the partners. The trust for the benefit of plaintiff's grandson had an option to purchase the interest of any of the other trusts at net book value.

Since the transfer was of an interest in the partnership and since the right to determine whether any trust should withdraw from the partnership was retained by the plaintiff and his son, the trusts were not free to remain out of the partnership. Since no partner could transfer his interest without the consent of all of the partners (including the plaintiff), none of the trusts was absolutely free to transfer its interest once the partnership was created. Nevertheless, the Court of Appeals, reviewing all of the facts and with the case of *Helvering v. Clifford* having been called to its attention, affirmed the judgment for the plaintiff.

Nicholas v. Davis, supra, concerned three successive partnerships, the second of which was a limited partnership. In the second partnership the limited part-

ners were the wives of the general partners. Each general partner gave his wife certain sums of money from the capital assets of the preceding partnership with the understanding among all of them that the gifts were to be used for the purchase of limited partners' interests in the second partnership. It appears that the limited partners could neither withdraw nor transfer their interests since the limited partnership agreement provided that it was to continue for a stated term and that the limited partners would be entitled to the return of their contributions upon the expiration of the term of the partnership, upon the dissolution of the partner or upon the consent of all of the other members of the partnership, both general and limited.

The Commissioner assessed a deficiency in income tax against one of the general partners on the theory that the income of his wife as a limited partner was in reality income of that general partner. The general partner concerned brought an action against a collector to recover the amount of the deficiency assessment paid, and the cause was tried before a jury. The plaintiff offered evidence showing, among other things, the facts set out above and the fact that the limited partner enjoyed complete dominion over her distributive share of partnership income, and the collector offered no evidence whatever. By direction of the trial court, a verdict was returned in favor of the plaintiff taxpayer. On appeal from a judgment entered thereon, the Court of Appeals for the Tenth

Circuit affirmed the judgment, holding that no question of credibility or issue of fact was presented for determination by a jury.

In each of the foregoing cases the challenged partner was not absolutely free to remain out of the partnership or to terminate or tranfer his interest once the partnership was created. On all of the facts in the record, however, those courts held the partnerships concerned to be bona fide recognizable partnerships for income tax purposes.

Given a case in which an examination of all of the evidence leaves doubt as to whether in fact and in law the donor of property has retained such control and dominion thereof as to render him liable for taxes on the income thereof under the doctrine of the *Clifford* case, the addition of the two factors mentioned could properly be sufficient to turn the decision in favor of taxability. It is respectfully submitted that such was the case in *Toor v. Westover, supra,* and that this court, in arriving at its decision in that case, did not base its determination solely upon those two factors, but rather, considering all of the circumstances, found a lack of true ownership in the transferee of the trust property. This rationale is not only borne out by this court's opinion, but also avoids the creation of a conflict of decision between this and the Eighth and Tenth Circuits.

CONCLUSION.

For the reasons set forth, the decisions of the Tax Court are correct and should be affirmed.

Dated, Honolulu, Hawaii,
November 2, 1953.

Respectfully submitted,
MILTON CADES,
Attorney for Respondents.

SMITH, WILD, BEEBE & CADES,
Of Counsel.

(Appendix Follows.)

Appendix.

Appendix

Internal Revenue Code:

Sec. 22. Gross Income

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, business, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U.S.C. 1946 ed., Sec. 22.)

Sec. 182. Tax of Partners.

In computing the net income of each partner, he shall include, whether or not distribution is made to him——

* * * * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

(26 U.S.C. 1946 ed., Sec. 182.)

Revised Laws of Hawaii (1935):

Chapter 225. Partnerships, Registration of.

* * * * * * *

Part 2. Special

Sec. 6870. *Between individuals.*—A partnership may be formed between two or more individuals for the transaction of any lawful business. A special partnership may be formed between one or more persons, called general partners, and one or more persons called special partners, for the transaction of any business.

* * * * * * *

Sec. 6880. *Only general partners act.*—The general partners only shall have authority to transact the business of a special partnership.

Sec. 6881. *Special partners may advise.*—A special partner may at all times investigate the partnership affairs and advise his partners or their agents as to their management.

Sec. 6882. *May loan money. Insolvency.*—A special partner may lend money to the partnership or advance money for it, or to it, and take from it security therefor, and as to such secured loans or advances has the same rights as any other creditor, but in case of the insolvency of the partnership all other claim which he may have against it must be postponed until all other creditors are satisfied.

Sec. 6883. *Receive interest and profits.*—A special partner may receive such lawful interest and such

proportion of profits as may be agreed upon, if not paid out of the capital invested in the partnership by him or some other special partner, and is not bound to refund the same to meet subsequent losses.

Sec. 6884. *May not withdraw capital.*—No special partner, under any pretense, may withdraw any part of the capital invested by him in the partnership during its continuance.

Sec. 6885. *Result of withdrawing capital.*—If a special partner withdraws capital from the firm, contrary to the provisions of sections 6883 or 6884, he thereby becomes a general partner.

* * * * * * *

LIABILITY OF PARTNERS.

* * * * * * *

Sec. 6887. *Of special partners.*—The contribution of a special partner to the capital of the firm, and the increase thereof, is liable for its debts; but he is not otherwise liable therefor, except as follows:

1. If he has wilfully made or permitted a false or materially defective statement in the certificate of the partnership, the affidavit filed therewith, or the published announcement thereof, he is liable as a general partner to all creditors of the firm; or,

2. If he has wilfully interfered with the business of the firm, except as permitted hereinabove, he is liable in like manner; or,

3. If he has wilfully joined in or assented to an act contrary to any of the provisions of sections 6880-6885, he is liable in like manner.

Sec. 6888. *For unintentional act.*—When a special partner has, unintentionally, done any of the acts mentioned in the last section, he is liable, as a general partner, to any creditor of the firm who has been actually misled thereby to his prejudice.

No. 13806

United States Court of Appeals

for the Ninth Circuit.

Docket 2793

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

ROY EATON,
Respondent.

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

GENEVIEVE H. EATON,
Respondent.

Transcript of Record

Petitions to Review Decisions of the Tax Court of the United States

FILED
JUL 23 1953
PAUL P. O'BRIEN
CLERK

Phillips & Van Orden Co., 870 Brannan Street, San Francisco, Calif.—7-10-53

No. 13806

United States
Court of Appeals
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COMMISSIONER OF INTERNAL REVENUE,
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES

For Petitioner:

MILTON CADES, ESQ.,
URBAN E. WILD, ESQ.,
J. RUSSELL CADES, ESQ.,
F. C. LOWELL HEAD, ESQ.

For Respondent:

CHARLES W. NYQUIST, ESQ.

Docket No. 24081

ROY EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1949

July 7—Petition received and filed. Taxpayer notified. Fee paid.

July 7—Request for Circuit hearing in Honolulu, T. H., filed by taxpayer. 7/19/49, granted.

July 7—Notice of appearance of Milton Cades, Urban E. Wild and J. Russell Cades, filed.

July 8—Copy of petition served on General Counsel.

The Tax Court of the United States

Aug. 23—Answer filed by General Counsel.

Aug. 30—Copy of Answer served on Taxpayer, Honolulu, T. H.

1951

Mar. 12—Hearing set June 13, 1951, Honolulu, T.H.

May 22—Hearing changed to June 15, 1951, Honolulu, T. H.

June 18—Hearing had before Judge Arundell on merits. Proceedings consolidated for hearing. Stipulation of facts with Exhibits 1 through 51 attached except #30 not used.

1951

Petitioner's Brief, August 17, 1951. Respondent's Brief, October 16, 1951. Petitioner's Reply, Nov. 30, 1951.

July 18—Transcript of Hearing 6/18/51, filed.

Aug. 16—Brief filed by taxpayer. Copy served.

Oct. 16—Reply Brief filed by General Counsel.

Oct. 22—Motion for extension to Jan. 29, 1952, to file reply brief, filed by taxpayer. 10/23/51 granted.

1952

Jan. 28—Reply brief filed by taxpayer. Copy served 1/29/52.

July 9—Memorandum Findings of Fact and Opinion rendered. Judge Arundell. Decision will be entered under Rule 50. Copy served.

Oct. 9—Respondent's computation for entry of decision filed.

Oct. 13—Hearing set November 19, 1952, at Washington, D. C., on Respondent's computation.

Oct. 30—Consent to Settlement, filed by taxpayer.

Oct. 31—Decision entered. Judge Arundell. Div. 7.

1953

Jan. 19—Petition for Review by U. S. Court of Appeals for the Ninth Circuit filed by General Counsel.

Feb. 6—Proof of Service on Counsel, filed.

Feb. 12—Motion for extension of time to 4/17/53 to transmit record, filed by General Counsel.

1953

Feb. 13—Order extending time to 4/17/53 to prepare, transmit and deliver record, entered.

Feb. 17—Entry of Appearance, F. C. Lowell Head, as counsel, filed.

Feb. 17—Proof of Service on Taxpayer, filed.

Apr. 2—Statement of Points filed by General Counsel, with proof of service thereon.

Apr. 2—Statement Re Diminution of Record filed by General Counsel, with proof of service thereon.

The Tax Court of the United States

Docket No. 24082

GENEVIEVE H. EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1949

July 7—Petition received and filed. Taxpayer notified. Fee paid.

July 7—Request for Circuit hearing in Honolulu, T.H., filed by Taxpayer. 7/19/49, granted.

July 7—Notice of appearance of Milton Cades, Urban E. Wild & J. Russell Cades, filed. 7/8/49, served.

1949

July 8—Copy of Petition served on General Counsel.

Aug. 24—Answer filed by General Counsel.

Sept. 1—Copy of Answer served on Taxpayer, Honolulu, T. H.

1951

Mar. 12—Hearing set June 13, 1951, Honolulu, T.H.

May 22—Hearing changed to June 15, 1951, Honolulu, T. H.

June 18—Hearing had before Judge Arundell on merits. Proceedings consolidated for hearing. Stipulation of facts with Exhibits 1 through 51 attached except #30 not used. Petitioner's Brief, August 17, 1951. Respondent's Brief, October 16, 1951. Petitioner's Reply, Nov. 30, 1951.

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1952

Jan. 28—Reply Brief filed by taxpayer. Copy served 1/29/52.

July 9—Memorandum Findings of Fact and Opinion rendered. Judge Arundell. Decision will be entered under Rule 50. Copy served.

Oct. 9—Respondent's computation for entry of decision filed.

1952

Oct. 13—Hearing set 11/19/52 at Washington, D. C., on Respondent's computation.

Oct. 30—Consent to Settlement, filed by taxpayer.

Oct. 31—Decision entered. Judge Arundell. Div. 7.

1953

Jan. 19—Petition for Review by U. S. Court of Appeals for the Ninth Circuit filed by General Counsel.

Feb. 6—Proof of Service on Counsel, filed.

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Apr. 2—Statement of Points filed by General Counsel, with proof of service thereon.

Apr. 2—Statement Re Diminution of Record filed by General Counsel, with proof of service thereon.

The Tax Court of the United States

Docket No. 24081

ROY EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IT:FC:LMJ-90D) dated April 28, 1949, and as a basis of his proceeding alleges as follows:

I.

The petitioner is an individual whose mailing address is Route #1, Box 303, Fullerton, California. The returns here involved were filed with the Collector for the Honolulu Division.

II.

The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to petitioner on April 28, 1949.

III.

The taxes in controversy are income taxes for the years and in the amounts shown below. The deficiency asserted is $50,798.30, the entire amount of which is in controversy:

Years	Deficiency
1943	$ 7,477.24
1944	23,589.24
1945	19,282.01
1946	449.81
	$50,798.30

IV.

The determination of tax set forth in said notice of deficiency is based on the following errors:

1. The Commissioner of Internal Revenue has erred in holding that Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942, hereinafter referred to as "Trust No. 1," was not, during the period October 1, 1942, to February 28, 1943, a bona fide special partner for income tax purposes of Nehi Beverage Company of Hawaii, a special partnership organized and doing business under the laws of the Territory of Hawaii, and that Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, hereinafter referred to as "Trust No. 2," was not, during the period March 1, 1943, to December 10, 1946, a bona fide special partner for income tax purposes of said partnership;

2. The Commissioner of Internal Revenue has erred in holding that all of the income of said Trust No. 1 and of said Trust No. 2, during the calendar years 1943 to 1946, inclusive, is the income of petitioner for income and victory tax pur-

poses, subject, however, to an adjustment under the Hawaiian Community Property Law commencing as of June 1, 1945;

3. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income and victory tax net income for the taxable year ended December 31, 1943, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $10,049.17, being the income received by Trust No. 1 from its interest in said partnership for said partnership's fiscal year ended February 28, 1943;

4. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income and victory tax net income for the taxable year ended December 31, 1943, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $7,574.90, being the income received by Trust No. 2 from its interest in said partnership for said partnership's fiscal year ended June 30, 1943;

5. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1943, by adding to the net gain reported by petitioner for said year the sum of $194.76, being the distributive share of the net capital gain of said partnership attributable to Trust No. 2 for said partnership's fiscal year ended June 30, 1943;

6. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $7,477.24, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1943;

7. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, by adding to the income reported by petitioner for said year from Nehi Beverage Company of Hawaii, the sum of $22,916.42, being the income received by Trust No. 2 from its interest in said partnership for said partnership's fiscal year ended June 30, 1944;

8. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, by adding to the income reported by petitioner for said year the sum of $750.00 received by Trust No. 1 as interest income during the calendar year 1944;

9. The Commissioner of Internal Revenue has erred in including in the determination of petitioner's income tax net income for the taxable year ended December 31, 1944, the sum of $5,509.08, representing the excess of expenses over the income from the operation of a sampan for commercial fishing purposes by said Nehi Beverage Company of Hawaii during said partnership's fiscal year ended June 30, 1944, which said amount is reflected

in the tax return filed by said partnership for that period;

10. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $23,589.24, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1944;

11. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1945, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $23,714.48 (less an adjustment of 1/24th thereof, being the amount allocable to Genevieve H. Eaton, wife of petitioner, based on the Hawaiian Community Property Law in effect as of June 1, 1945), being the income received by Trust No. 2 from its interest in said partnership for said partnership's fiscal year ended June 30, 1945;

12. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1945, by adding to the income reported by petitioner for said year, the sum of $750.00 received by Trust No. 1 as interest income during the calendar year 1945;

13. The Commissioner of Internal Revenue has erred in including in the determination of petitioner's income tax net income for the taxable year

ended December 31, 1945, the sum of $1,004.37, representing the excess of expenses over the income from the operation of a sampan for commercial fishing purposes by said Nehi Beverage Company of Hawaii during said partnership's fiscal year ended June 30, 1945 (less an adjustment of 1/24th thereof, being the amount allocable to Genevieve H. Eaton, wife of petitioner, based on the Hawaiian Community Property Law in effect as of June 1, 1945, and a further adjustment to eliminate the net capital gain reported on the return of petitioner for that year from the sale of the sampan by Nehi Beverage Company of Hawaii in the amount of $261.33), which said amount is reflected in the tax return filed by said partnership for that period;

14. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $19,282.01, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1945;

15. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $222.03, being one-half of the income received by Trust No. 2 from its interest in said partnership for said partnership's fiscal periods ended June 30, 1946 and December 10, 1946;

16. The Commissioner of Internal Revenue has

erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the income reported by petitioner for said year, the sum of $691.60, being one-half of the income received by Trust No. 1 from investments during the calendar year 1946;

17. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the net gain reported by petitioner for said year, the sum of $637.93, being one-half of the distributive share of the net capital gain of said Nehi Beverage Company of Hawaii attributable to Trust No. 2 for said partnership's fiscal periods ended June 30, 1946, and December 10, 1946;

18. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $449.81, or of any part thereof, in petitioner's income tax for the taxable year ended December 31, 1946.

V.

The facts upon which petitioner relies as a basis for this proceeding are as follows:

1. The petitioner, on September 30, 1942, settled a Trust, hereinafter referred to as "Trust No. 1," by a transfer to Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, of a sum of Fifteen Thousand Dollars ($15,000.00) under the hereinafter mentioned terms of said Trust Agreement;

2. By the terms of said Trust Agreement, the Trustee was to contribute the said sum of Fifteen Thousand Dollars ($15,000.00) to the capital of Nehi Beverage Company of Hawaii, a special partnership duly organized under the terms of a special partnership agreement dated September 30, 1942, for a thirty per cent (30%) interest therein, and to continue to be a special partner in such partnership; said contributed capital being the fair and reasonable value of said interest duly ascertained as of September 30, 1942;

3. By the terms of said Trust Agreement, all of the income was to be accumulated until the youngest of the children of the Settlor reached the age of twenty-five (25) years, with discretion in the Trustee to pay out of the net income of the Trust amounts necessary for the support, maintenance and education of the beneficiaries;

4. By the terms of said Trust Agreement, the petitioner, as Settlor, completely divested himself of all right, title or interest in the trust estate, both corpus and income;

5. By the terms of said Trust Agreement, the Trustee has no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever to or at the direction of the petitioner; such right of disposition being confined to the terms of the trust instrument and to be exercised where permissible under the terms of the Trust within the sole discretion of the Trustee;

6. The gross income of said Trust No. 1, for the taxable year 1943, included income from the partnership of Nehi Beverage Company of Hawaii in the amount of $10,049.17, which income was reported by said Trust for the year 1943, the income and victory tax was computed thereon, and said tax was properly paid by the said Trust;

7. The gross income of the said Trust No. 1, for the taxable year 1944, included income from interest in the amount of $750.00, which income was reported by said Trust for the year 1944, the net income for income tax purposes was computed thereon by the said Trust, and said tax was properly paid by the said Trust;

8. The gross income of the said Trust No. 1, for the taxable year 1945, included income from interest in the amount of $750.00, which income was reported by said Trust for the year 1945, the net income for income tax purposes was computed thereon by the said trust, and said tax was properly paid by the said Trust;

9. The gross income of the said Trust No. 1, for the taxable year 1946, included investment income in the amount of $1,383.20, which income was reported by said Trust for the year 1946, the net income for income tax purposes was computed thereon by said Trust, and said tax was properly paid by the said Trust;

10. The petitioner, on February 28, 1943, settled a Trust, hereinafter referred to as "Trust No. 2," by a transfer to said Bishop Trust Company, Lim-

ited, as Trustee, of a sum of Fifteen Thousand Dollars ($15,000.00), under the hereinafter mentioned terms and conditions;

11. By the terms of said Trust Agreement, a thirty per cent (30%) capital interest in the partnership known as Nehi Beverage Company of Hawaii was to be acquired for Fifteen Thousand Dollars ($15,000.00); said amount being the fair and reasonable value of said interest ascertained as of February 28, 1943;

12. The terms of said Trust Agreement were practically identical with the provisions of said Trust No. 1, except that the Trustee was required to accumulate all income until the youngest of the children of the Settlor reached the age of twenty-five (25) years, without any discretion to distribute any portion of the income or principal for the support, maintenance and education of the beneficiaries;

13. As of February 28, 1943, Trust No. 2 purchased from said Trust No. 1 its interest as a special partner in said Nehi Beverage Company of Hawaii, and continued to be a partner in the new special partnership with the same name organized as of that time.

14. The gross income of said Trust No. 2, for the taxable year 1943, included income from said partnership in the amount of $7,574.90, and a net capital gain of the said partnership in the amount of $194.76, all of which income was reported by said Trust No. 2 for the year 1943, the income tax and

victory tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

15. The gross income of said Trust No. 2 for the taxable year 1944, included income from said partnership in the amount of $22,916.42, which income was reported by said Trust No. 2 for the year 1944, the income tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

16. The gross income of said Trust No. 2, for the taxable year 1945, included income from said partnership in the amount of $23,714.38, which income was reported by said Trust No. 2 for the year 1945, the income tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

17. The gross income of said Trust No. 2 for the taxable year 1946, included income from said partnership in the amount of $446.06, and a net capital gain of said partnership in the amount of $1,275.86, all of which income was reported by said Trust No. 2 for the year 1946, the income tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

18. In 1943, Nehi Beverage Company of Hawaii purchased a sampan for the purpose of conducting what appeared to be a profitable side line business in commercial fishing, and for the additional purpose of retaining the services of a valued employee of the bottling business;

19. Because of the requirement of heavy repairs and maintenance, and the deterioration of the fish-

ing grounds by reason of gun practice and other activities of the military forces of the United States, Nehi Beverage Company of Hawaii suffered a net operating loss on the sampan in the amount of $5,509.08 during its fiscal year ended June 30, 1944, which was claimed as a deduction by said Nehi Beverage Company of Hawaii in computing its income tax net income on its return for that fiscal year, which, in turn, was used in computing the net income of petitioner subject to tax for the year 1944;

20. A similar net operating loss on the sampan, in the amount of $1,004.37, was incurred during said Partnership's fiscal year ended June 30, 1945, which was claimed as a deduction by said partnership in computing its income tax net income on its return for that fiscal year, which in turn, was used in computing the net income of petitioner subject to tax for the year 1945;

21. Said sampan was not used by the partnership or others for pleasure purposes during the period it was owned by said Nehi Beverage Company of Hawaii, but was used solely for commercial fishing purposes;

22. That Nehi Beverage Company of Hawaii, a special partnership organized and doing business under the laws of the Territory of Hawaii, composed of Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., general partners, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942, special partner, elected to file

its tax returns on an accrual and fiscal year basis ending on the 28th day of February, and filed its first return on that basis for the fiscal year ending February 28, 1943;

23. That Nehi Beverage Company of Hawaii, a special partnership organized and doing business under the laws of the Territory of Hawaii, composed of Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., general partners, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, special partner, elected to file its tax returns on an accrual and fiscal year basis ending on the 30th day of June of each and every year, and filed its first return on that basis for the fiscal year ended June 30, 1943; that said partnership was dissolved and filed its final return for the fiscal period ending December 10, 1946.

Wherefore Petitioner Prays that this Court may hear the proceeding and determine that there is no deficiency due from the petitioner for the years 1943, 1944, 1945 and 1946.

/s/ ROY EATON,
Petitioner.

MILTON CADES,
URBAN E. WILD,
J. RUSSELL CADES,
400 Bishop Trust Building,
Honolulu, T. H.,
Counsel for Petitioner.

State of California,
County of Orange—ss.

Roy Eaton, being duly sworn, says that he is the petitioner above named; that he has read the foregoing petition, or had the same read to him, and is familiar with the statements contained therein; that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

/s/ ROY EATON.

Subscribed and sworn to before me this 5th day of July, 1949.

[Seal] /s/ P. B. HESS,
Notary Public in and for the County of Orange, State of California.

My Commission expires Nov. 14, 1949.

EXHIBIT "A"

Form 1230. SN-IT-1.
IT:FC:LMJ—90D.

Apr. 28, 1949.

Mr. Roy Eaton,
Route #1, Box 303,
Fullerton, California.

Dear Sir:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1943; December 31, 1944; December 31, 1945, and December 31, 1946, discloses a de-

ficiency of $50,798.30, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the 90th day from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P. O. Box 421, Honolulu 9, T. H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner.

By /s/ H. A. PETERSON,
Internal Revenue Agent
in Charge.

Enclosures:

Statement,
Form 1276,
Form of Waiver.

STATEMENT

Mr. Roy Eaton
Route No. 1, Box 303,
Fullerton, California

Year	Deficiency
1943	$ 7,477.24
1944	23,589.24
1945	19,282.01
1946	449.81
Total	$50,798.30

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated September 30, 1947, to your protest dated July 14, 1948; and to the statements made at the conference held on March 8, 1949.

A copy of this letter and statement has been mailed to your representative, Mr. Milton Cades, of Smith, Wild, Beebe and Cades, Post Office Box 224, Honolulu, T. H., in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1942

Adjustments to Net Income

Net income as disclosed by return	$64,034.88
Unallowable deductions and additional income	none
Net income adjusted	$64,034.88

Computation of Tax

Net income adjusted		$64,034.88
Less: Personal exemption	$ 1,200.00	
Credit for dependents	1,050.00	2,250.00
Balance (Surtax net income)		$61,784.88
Less: Earned income credit:		
10 per cent of 20 per cent of $61,911.76		1,238.24
Balance subject to normal tax		$60,546.64
Normal tax at 6% on $60,546.64		$ 3,632.80
Surtax on $61,784.88		31,071.57
Income tax liability		$34,704.37

Taxable Year Ended December 31, 1943

Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return	$51,817.38	$52,583.91
Unallowable deductions and additional income:		
(a) Partnership income	17,624.07	17,624.07
(b) Net long term capital gain	194.76	
(c) Mathematical error	30.00	
Total	$69,666.21	$70,207.98
Nontaxable income and additional deductions:		
(d) Contributions	243.34	
(e) Other deductions	125.00	125.00
Total	$ 368.34	$ 125.00
Net income adjusted	$69,297.87	$70,082.98

Explanation of Adjustments

(a) Represents income of the partnership, Nehi Beverage Company of Hawaii, which is held to be taxable to you, and which was reported on fiduciary returns filed for Roy Eaton Trusts No. 1 and No. 2, as follows:

Roy Eaton Trust No. 1	$10,049.17
Roy Eaton Trust No. 2	7,574.90
Total	$17,624.07

(b) Represents net capital gain of the partnership, Nehi Beverage Company of Hawaii, which was reported by Roy Eaton Trust No. 2 on a fiduciary return, and is held to be taxable to you. Net capital gains are not includible in victory tax net income.

(c) Represents an error in addition of the deductions on your 1943 return which should be $2,944.44 instead of $2,974.44. The difference of $30.00 is adjusted here. No adjustment need be made for victory tax net income purposes.

(d) Represents contributions of the partnership, Nehi Beverage Company of Hawaii, which were reported on fiduciary returns filed for Roy Eaton Trusts No. 1 and No. 2, as follows:

Roy Eaton Trust No. 1	$176.67
Roy Eaton Trust No. 2	66.67
Total	$243.34

Contributions are deductible on your return since the income from the partnership reported by the trusts is held to be taxable to you. Contributions are not deductible from victory tax net income.

(c) Represents trustee's expenses deducted by Roy Eaton Trusts No. 1. Since the income of the trusts is held to be taxable to you, the trustee's commissions are deductible on your return.

Computation of Alternative Tax

Net income adjusted		$69,297.87
Less: Net long-term capital gain		2,402.67
Ordinary net income		$66,895.20
Less: Personal exemption	$1,200.00	
Credit for dependents	1,050.00	2,250.00
Surtax net income		$64,645.20
Less: Earned income credit (10% of 20% of $64,122.24)		1,282.44
Balance subject to normal tax		$63,362.76
Normal tax at 6% on $63,362.76		$ 3,801.77
Surtax on $64,645.20		33,045.19
Partial tax		$36,846.96
Plus: 50% of net capital gain of $2,402.67		1,201.34
Alternative tax		$38,048.30

Computation of Income and Victory Tax

Income tax net income adjusted		$69,297.87
Less: Personal exemption	$1,200.00	
Credit for dependents	1,050.00	2,250.00
Surtax net income		$67,047.87
Less: Earned income credit (10% of 20% of $64,122.24)		1,282.44
Balance subject to normal tax		$65,765.43
Normal tax at 6% on $65,765.43		$ 3,945.93
Surtax on $67,047.87		34,703.03
Total income tax		$38,648.96

Balance of income tax (total income tax or alternative tax, whichever is smaller)		$38,048.30
Victory tax net income	$70,082.98	
Less: Specific exemption	624.00	
Income subject to victory tax	$69,458.98	
Victory tax before credit (5% of $69,458.98)	$ 3,472.95	
Less: Victory tax credit — maximum	1,300.00	
Net victory tax		$ 2,172.95
Net income tax and victory tax (1)		$40,221.25
Income tax for 1942 (2)		$34,704.37
Amount of item (1) or (2) whichever is larger		$40,221.25
Forgiveness feature:		
(a) Amount of item (1) or (2) whichever is smaller	$34,704.37	
(b) Amount forgiven — 75% of $34,704.37	26,028.28	
(c) Amount unforgiven		8,676.09
Correct income and victory tax liability		$48,897.34
Income and victory tax liability disclosed by return, Account No. 351588		41,720.10
Deficiency in income and victory tax		$ 7,477.24

Taxable Year Ended December 31, 1944

Adjustments to Net Income

Net income as disclosed by return		$64,348.79
Unallowable deductions and additional income:		
(a) Partnership income	$28,425.50	
(b) Trust income	750.00	29,175.50
Total		$93,524.29

Nontaxable income and additional deductions:		
(c) Contributions	$ 308.33	
(d) Taxes	341.13	
(e) Trustee's commissions	505.00	$ 1,154.46
Net income adjusted		$92,369.83

Explanation of Adjustments

(a) Represents income of the partnership, Nehi Beverage Company of Hawaii, which is held to be taxable to you, consisting of the following items:

(1) Amount reported on fiduciary return filed for Roy Eaton Trust No. 2:	$22,916.42
(2) Amount claimed on the partnership return as net sampan operating losses and disallowed as unallowable deduction	5,509.08
Total	$28,425.50

(b) Represents interest income reported on a fiduciary return by Roy Eaton Trust No. 1, which is held taxable to you.

(c) Represents contributions of the partnership, Nehi Beverage Company of Hawaii, which were deducted on fiduciary return filed for Roy Eaton Trust No. 2, and which are deductible on your return since the income from the partnership reported by the trust is held to be taxable to you.

(d) Represents taxes paid by the partnership, Nehi Beverage Company of Hawaii, in the amount of $147.44, which were deducted on fiduciary return filed for Roy Eaton Trust No. 2; and taxes paid by Roy Eaton Trust No. 1 in the amount of $193.69 and deducted on a fiduciary return filed for the trust. Since the income from the partnership reported by Trust No. 2 and the interest income reported by Trust No. 1 is held to be taxable to you, the above taxes are deductible on your return.

(e) Represents trustee's commissions deducted by Roy Eaton Trust No. 1 in the amount of $90.00, and by Roy Eaton Trust No. 2 in the amount of $415.00, on fiduciary returns. Since the income reported by the trusts on fiduciary returns is held to be taxable to you, the trustee's commissions above are deductible on your return.

Computation of Tax

Net income adjusted	$92,369.83	
Less: Surtax exemption	2,500.00	
Surtax net income	$89,869.83	
Surtax on $89,869.83		$58,510.66
Net income adjusted	$92,369.83	
Less: Normal tax exemption	500.00	
Balance subject to normal tax	$91,869.83	
Normal tax at 3%		2,756.09
Correct income tax liability		$61,266.75
Income tax liability disclosed by return, Account No. 300438		37,677.51
Deficiency in income tax		$23,589.24

Taxable Year Ended December 31, 1945

Adjustments to Net Income

Net income as disclosed by return		$69,741.95
Unallowable deductions and additional income:		
(a) Partnership income	$23,688.80	
(b) Trust income	750.00	24,438.80
Total		$94,180.75
Nontaxable income and additional deductions:		
(c) Net capital gains	$ 261.33	
(d) Contributions	366.67	
(e) Taxes	494.00	
(f) Trustee's commissions	500.00	1,622.00
Net income adjusted		$92,558.75

Explanation of Adjustments

(a) Represents income of the partnership, Nehi Beverage Company of Hawaii, which is held to be taxable to you, consisting of the following items:

(1) Amount reported on fiduciary return filed for Roy Eaton Trust No. 2:	$23,714.38
(2) Amount claimed on the partnership return as sampan operating losses and disallowed as unallowable deduction	1,004.37
Total	$24,718.75
(3) Less: Amount allocable to Mrs. Genevieve H. Eaton based on the Hawaii Community Property Law in effect as of June 1, 1945, with the partnership reporting on a fiscal year basis ending June 30, 1945: 1/2 of 1/12th, or 1/24th of $24,718.75, or	1,029.95
Adjustment as above	$23,688.80

(b) Represents interest income reported on a fiduciary return by Roy Eaton Trust No. 1, which is held to be taxable to you. This amount was received prior to the date on which the Hawaii Community Property Law went into effect.

(c) Represents the net capital gain reported on your return from the sale of the sampan by the partnership, Nehi Beverage Company of Hawaii. The total net capital gain from the sale of the sampan amounted to $392.00 of which $261.33 were allocated to you and $130.67 to Roy Eaton Trust No. 2. The total gain is thus eliminated as offset against the sampan operating losses.

(d) Represents contributions of the partnership, Nehi Beverage Company of Hawaii, which were deducted on fiduciary return filed for Roy Eaton Trust No. 2, and which are deductible on your return since the income from the partnership reported by the trust is held taxable to you.

(e) Represents taxes paid by the partnership, Nehi Beverage Company of Hawaii, which were deducted on fiduciary return filed for Roy Eaton Trust No. 2, and which are deductible on your return since the income from the partnership reported by the trust is held to be taxable to you.

(f) Represents trustee's commissions deducted by Roy Eaton Trust No. 1 in the amount of $175.00, and by Roy Eaton Trust No. 2 in the amount of $325.00, on fiduciary returns. Since the income reported by the trusts on fiduciary returns is held to be taxable to you, the trustee's commission's above are deductible on your return.

Computation of Alternative Tax

Net income adjusted	$92,558.75	
Less: Net long-term capital gain	3,568.78	
Ordinary net income	$88,989.97	
Less: Surtax exemption	2,000.00	
Surtax net income	$86,989.97	
Surtax on $86,989.97		$56,091.57
Ordinary net income	$88,989.97	
Less: Normal tax exemption	500.00	
Balance subject to normal tax	$88,489.97	
Normal tax at 3% on $88,489.97		2,654.70
Partial tax		$58,746.27
Plus: 50% of net capital gain of $3,568.78		1,784.39
Alternative tax		$60,530.66

Computation of Tax

Net income adjusted	$92,558.75	
Less: Surtax exemption	2,000.00	
Surtax net income	$90,558.75	
Surtax on $90,558.75		$59,106.11
Net income adjusted	$92,558.75	
Less: Normal tax exemption	500.00	
Balance subject to normal tax	$92,058.75	
Normal tax at 3% on $92,058.75		2,761.76
Total income tax		$61,867.87
Correct income tax liability		$60,530.66
Income tax liability disclosed by return, Account No. 300635		41,248.65
Deficiency in income tax		$19,282.01

Taxable Year Ended December 31, 1946

Adjustments to Net Income

Net Income as disclosed by return		$27,276.30
Unallowable deductions and additional income:		
(a) Partnership income	$223.03	
(b) Net long-term capital gain	637.93	
(c) Trust income	691.60	1,552.56
Total		$28,828.86
Nontaxable income and additional deductions:		
(d) Contributions	$184.84	
(e) Taxes	155.09	
(f) Trustee's commissions	281.64	621.57
Net income adjusted		$28,207.29

Explanation of Adjustments

(a) Represents income of the partnership Nehi Beverage Company of Hawaii, which is held to be taxable to you, and which was reported on fiduciary return filed for Roy Eaton Trust No. 2. Of the total amount of $446.06, one-half, or $223.03, is allocable to Mrs. Genevieve H. Eaton under the Hawaii Community Property Law.

(b) Represents the portion of the net capital gains of the Nehi Beverage Company of Hawaii reported on a fiduciary return filed for Roy Eaton Trust No. 2 which is held to be taxable to you. Of the total amount of $1,275.86, one-half, or $637.93, is allocated to Mrs. Genevieve H. Eaton.

(c) Represents income reported on a fiduciary return by Roy Eaton Trust No. 1, which is held to be taxable to you. Of the total amount of $1,383.20, one-half, or $691.60, is allocated to Mrs. Genevieve H. Eaton.

(d) Represents contributions of the partnership, Nehi Beverage Company of Hawaii, which were deducted in the amount of $258.29 on fiduciary return filed for Roy Eaton Trust No. 2, and which are deductible on your return since the income from the partnership reported by the trust is held to be taxable to you. The correct amount of allowable contributions, as shown on the partnership returns, is $369.67, of which one-half, or $184.83, is allocated to Mrs. Genevieve H. Eaton.

(e) Represents taxes paid by the partnership, Nehi Beverage Company of Hawaii, in the amount of $308.47, which were deducted on fiduciary return filed for Roy Eaton Trust No. 2; and taxes paid by Roy Eaton Trust No. 1 in the amount of $1.72 and deducted on a fiduciary return filed for the trust. Since the income from the partnership reported by Trust No. 2 and the income reported by Trust No. 1 is held to be taxable to you, the above taxes are deductible on your return. Of the total amount of $310.19, one-half, or $155.10, is allocated to Mrs. Genevieve H. Eaton.

(f) Represents trustee's commissions deducted by Roy Eaton Trust No. 1 in the amount of $88.29, and by Roy Eaton Trust No. 2 in the amount of $475.00, on fiduciary returns. Since the income reported by the trusts on fiduciary returns is held to be taxable to you, the trustee's commissions are deductible on your return. Of the total amount of $563.29, one-half, or $281.65, is allocated to Mrs. Genevieve H. Eaton.

Computation of Alternative Tax

Net income adjusted	$28,207.29
Less: Net long-term capital gain	11,783.16
Ordinary net income	$16,424.13
Less: Exemptions	1,500.00
Taxable income	$14,924.13
Combined tentative normal tax and surtax on $14,924.13	$ 4,694.34
Less: 5% of $4,694.34	234.72
Partial tax	$ 4,459.62
Plus: 50% of net capital gain of $11,783.16	5,891.58
Alternative tax	$10,351.20

Computation of Tax

Net income adjusted	$28,207.29
Less: Exemptions	1,500.00
Taxable income	$26,707.29

Combined tentative normal tax and surtax on $26,707.29	$11,178.52
Less: 5% of $11,178.52	558.93
Combined normal tax and surtax	$10,619.59
Correct income tax liability	$10,351.20
Income tax liability disclosed by return, Account No. 300298	9,901.39
Deficiency in income tax	$ 449.81

Received and Filed July 7, 1949, T.C.U.S.

[Title of Tax Court and Cause.]

Docket No. 24081

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I. and II.

Admits the allegations contained in Paragraphs I and II of the petition.

III.

Admits the allegations contained in Paragraph III of the petition, except denies that the entire amount of the deficiency is in controversy.

IV.

1 to 18, inclusive. Denies that the Commissioner erred in the determination of the deficiency as alleged in Paragraph IV of the petition and Subparagraphs 1 to 18, inclusive, thereunder.

V.

1. Admits that the petitioner, on September 30, 1942, settled a Trust, hereinafter referred to as "Trust No. 1," by a transfer to Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, of a sum of Fifteen Thousand Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 1 of Paragraph V of the petition.

2. Admits that by the terms of said Trust Agreement, the Trustee was to contribute the said sum of Fifteen Thousand Dollars ($15,000.00) to the capital of Nehi Beverage Company of Hawaii; denies the remaining allegations contained in Subparagraph 2 of Paragraph V of the petition.

3. Admits the allegations contained in Subparagraph 3 of Paragraph V of the petition.

4 and 5. Denies the allegations contained in Subparagraphs 4 and 5 of Paragraph V of the petition.

6. Admits that the gross income reported by Trust No. 1, for the taxable year 1943, included one item designated as income from the partnership of Nehi Beverage Company of Hawaii in the amount of $10,049.17; denies the remaining allegations contained in Subparagraph 6 of Paragraph V of the petition.

7. Admits that the gross income reported by Trust No. 1, for the taxable year 1944, included an item designated interest in the amount of $750.00; denies the remaining allegations contained in Subparagraph 7 of Paragraph V of the petition.

8. Admits that the gross income reported by Trust No. 1, for the taxable year 1945, included an item designated interest in the amount of $750.00; denies the remaining allegations contained in Subparagraph 8 of Paragraph V of the petition.

9. Admits that the gross income reported by Trust No. 1, for the taxable year 1946, included an item designated as investment income in the amount of $1,383.20; denies the remaining allegations contained in Subparagraph 9 of Paragraph V of the petition.

10. Admits that the petitioner, on February 28, 1943, settled a Trust, hereinafter referred to as "Trust No. 2," by a transfer to said Bishop Trust Company, Limited, as Trustee, of a sum of Fifteen Thousand Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 10 of Paragraph V of the petition.

11. Admits that by the terms of said Trust Agreement, a thirty per cent (30%) capital interest in Nehi Beverage Company of Hawaii was to be acquired for Fifteen Thousand Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 11 of Paragraph V of the petition.

12. Admits that under the terms of said Trust

Agreement the Trustee was required to accumulate all income until the youngest of the children of the Settlor reached the age of twenty-five (25) years, without any discretion to distribute any portion of the income or principal for the support, maintenance and education of the beneficiaries; denies the remaining allegations contained in Subparagraph 12 of Paragraph V of the petition.

13. Admits that as of February 28, 1943, Trust No. 2 purchased from said Trust No. 1 its interest as an alleged special partner in said Nehi Beverage Company of Hawaii; denies the remaining allegations contained in Subparagraph 13 of Paragraph V of the petition.

14. Admits that the gross income reported by Trust No. 2, for the taxable year 1943, included an item designated as income from said partnership in the amount of $7,574.90, and a net capital gain of the said partnership in the amount of $194.76; denies the remaining allegations contained in Subparagraph 14 of Paragraph V of the petition.

15. Admits that the gross income reported by Trust No. 2, for the taxable year 1944, included an item designated as income from said partnership in the amount of $22,916.42; denies the remaining allegations contained in Subparagraph 15 of Paragraph V of the petition.

16. Admits that the gross income reported by Trust No. 2, for the taxable year 1945, included an item designated as income from said partnership

in the amount of $23,714.38; denies the remaining allegations contained in Subparagraph 16 of Paragraph V of the petition.

17. Admits that the gross income reported by Trust No. 2, for the taxable year 1946, included an item designated as income from said partnership in the amount of $446.06, and a net capital gain of said partnership in the amount of $1,275.86; denies the remaining allegations contained in Subparagraph 17 of Paragraph V of the petition.

18. Admits that Nehi Beverage Company of Hawaii purchased a sampan; denies the remaining allegations contained in Subparagraph 18 of Paragraph V of the petition.

19. Admits that Nehi Beverage Company of Hawaii claimed a deduction of $5,509.08 in computing its income tax net income on its return for the fiscal year ended June 30, 1944, which, in turn, was used in computing the net income of petitioner subject to tax for the year 1944; denies the remaining allegations contained in Subparagraph 19 of Paragraph V of the petition.

20. Admits that a similar deduction was claimed by said partnership in computing its income tax net income on its return for the fiscal year ended June 30, 1945, which, in turn, was used in computing the net income of petitioner subject to tax for the year 1945; denies the remaining allegations contained in Subparagraph 20 of Paragraph V of the petition.

21. Denies the allegations contained in Subparagraph 21 of Paragraph V of the petition.

22. Admits that Nehi Beverage Company of Hawaii filed its first return for the fiscal year ending February 28, 1943; denies the remaining allegations contained in Subparagraph 22 of Paragraph V of the petition.

23. Admits that Nehi Beverage Company of Hawaii filed a return for the fiscal year ended June 30, 1943, and filed its final return for the fiscal period ending December 10, 1946; denies the remaining allegations contained in Subparagraph 23 of Paragraph V of the petition.

VI.

Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of
Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;
T. M. MATHER,
LEONARD A. MARCUSSEN,
Special Attorneys, Bureau of
Internal Revenue.

Received and filed August 23, 1949, T.C.U.S.

The Tax Court of the United States

Docket No. 24082

GENEVIEVE H. EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IT:FC:LMJ—90D) dated April 28, 1949, and as a basis of her proceeding alleges as follows:

I.

The petitioner is an individual whose mailing address is Route #1, Box 303, Fullerton, California. The returns here involved were filed with the Collector for the Honolulu Division.

II.

The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to petitioner on April 28, 1949.

III.

The taxes in controversy are income taxes for the years and in the amounts shown below. The deficiency asserted is $830.90, the entire amount of which is in controversy.

Years	Deficiency
1945	$381.09
1946	449.81
	$830.90

IV.

The determination of tax set forth in said notice of deficiency is based on the following errors:

1. The Commissioner of Internal Revenue has erred in holding that Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, hereinafter referred to as "Trust No. 2," was not, during the period July 1, 1944, to December 10, 1946, a bona fide special partner for income tax purposes of Nehi Beverage Company of Hawaii, a special partnership organized and doing business under the laws of the Territory of Hawaii;

2. The Commissioner of Internal Revenue has erred in holding that all the income of Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942, hereinafter referred to as "Trust No. 1," during the calendar year 1946, and all of the income of said Trust No. 2 during the calendar years 1945 and 1946, is the income of said Roy Eaton, husband of petitioner, for income tax purposes, and, from and after June 1, 1945, by virtue of the Hawaiian Community Property Law, one-half thereof is taxable to petitioner;

3. The Commissioner of Internal Revenue has

erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1945, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $988.00 received by Trust No. 2 as income from its interest in said partnership for said partnership's fiscal year ended June 30, 1945, and allocable to petitioner based on the Hawaiian Community Property Law in effect as of June 1, 1945;

4. The Commissioner of Internal Revenue has erred in including in the determination of petitioner's income tax net income for the taxable year ended December 31, 1945, the sum of $41.85, representing the portion allocable to petitioner based on the Hawaiian Community Property Law in effect as of June 1, 1945, of the excess of expenses over the income from the operation of a sampan for commercial fishing purposes by said Nehi Beverage Company of Hawaii during said partnership's fiscal year ended June 30, 1945, which said amount is reflected in the tax return filed by said partnership for that period;

5. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $381.09, or of any part thereof, in the petitioner's income tax for the taxable year ended December 31, 1945;

6. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended Decem-

ber 31, 1946, by adding to the income reported by petitioner for said year from said Nehi Beverage Company of Hawaii, the sum of $222.03, being one-half of the income received by Trust No. 2 from its interest in said partnership for said partnership's fiscal periods ended June 30, 1946, and December 10, 1946;

7. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the income reported by petitioner for said year, the sum of $691.60, being one-half of the income received by Trust No. 1 from investments during the calendar year 1946;

8. The Commissioner of Internal Revenue has erred in the determination of petitioner's income tax net income for the taxable year ended December 31, 1946, by adding to the net gain reported by petitioner for said year, the sum of $637.93, being one-half of the distributive share of the net capital gain of said Nehi Beverage Company of Hawaii, attributable to Trust No. 2 for said partnership's fiscal periods ended June 30, 1946, and December 10, 1946;

9. The Commissioner of Internal Revenue has erred in determining that there is a deficiency of $449.81, or of any part thereof, in petitioner's income tax for the taxable year ended December 31, 1946.

V.

The facts upon which petitioner relies as a basis for this proceeding are as follows:

1. Roy Eaton, the husband of petitioner, on September 30, 1942, settled Trust No. 1, by a transfer to Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, of a sum of Fifteen Thousand Dollars ($15,000.00) under the hereinafter-mentioned terms of said Trust Agreement;

2. By the terms of said Trust Agreement, the Trustee was to contribute the said sum of Fifteen Thousand Dollars ($15,000.00) to the capital of Nehi Beverage Company of Hawaii, a special partnership duly organized under the terms of a special partnership agreement dated September 30, 1942, for a thirty per cent (30%) interest therein, and to continue to be a special partner in such partnership; said contributed capital being the fair and reasonable value of said interest duly ascertained as of September 30, 1942;

3. By the terms of said Trust Agreement, all the income was to be accumulated until the youngest of the children of the Settlor reached the age of twenty-five (25) years, with discretion in the Trustee to pay out of the net income of the Trust amounts necessary for the support, maintenance and education of the beneficiaries;

4. By the terms of said Trust Agreement, the said Roy Eaton, as Settlor, completely divested

himself of all right, title or interest in the trust estate, both corpus and income;

5. By the terms of said Trust Agreement, the Trustee has no right or power, discretionary or otherwise, to make any distribution of income or principal, current or accumulated, in any manner whatsoever to or at the direction of said Roy Eaton; such right of disposition being confined to the terms of the trust instrument and to be exercised where permissible under the terms of the Trust within the sole discretion of the Trustee;

6. The gross income of the said Trust No. 1, for the taxable year 1946, included investment income in the amount of $1,383.20, which income was reported by said Trust for the year 1946, the net income for income tax purposes was computed thereon by said Trust, and said tax was properly paid by the said Trust;

7. The said Roy Eaton, on February 28, 1943, settled Trust No. 2 by a transfer to said Bishop Trust Company, Limited, as Trustee, of a sum of Fifteen Thousand Dollars ($15,000.00) under the hereinafter-mentioned terms and conditions;

8. By the terms of said Trust Agreement, a thirty per cent (30%) capital interest in the partnership known as Nehi Beverage Company of Hawaii was to be acquired for Fifteen Thousand Dollars ($15,000.00); said amount being the fair and reasonable value of said interest ascertained as of February 28, 1943;

9. The terms of said Trust Agreement were practically identical with the provisions of said Trust No. 1, except that the Trustee was required to accumulate all income until the youngest of the children of the Settlor reached the age of twenty-five (25) years, without any discretion to distribute any portion of the income or principal for the support, maintenance and education of the beneficiaries;

10. As of February 28, 1943, Trust No. 2 purchased from Trust No. 1 its interest as a special partner in said Nehi Beverage Company of Hawaii, and continued to be a partner in the new special partnership with the same name organized as of that time;

11. The gross income of said Trust No. 2, for the taxable year 1945, included income from said partnership in the amount of $23,714.38, which income was reported by said Trust No. 2 for the year 1945, the income tax of said Trust was computed thereon and said tax was properly paid by said Trust;

12. The gross income of said Trust No. 2, for the taxable year 1946, included income from said partnership, in the amount of $446.06, and a net capital gain of said partnership in the amount of $1,275.86, all of which income was reported by said Trust No. 2 for the year 1946, the income tax of said Trust was computed thereon, and said tax was properly paid by said Trust;

13. In 1943, Nehi Beverage Company of Hawaii purchased a sampan for the purpose of conducting what appeared to be a profitable sideline business in commercial fishing, and for the additional purpose of retaining the services of a valued employee of the bottling business;

14. Because of the requirement of heavy repairs and maintenance, and the deterioration of the fishing grounds by reason of gun practice and other activities of the military forces of the United States, Nehi Beverage Company of Hawaii suffered a net operating loss on the sampan in the amount of $1,004.37 during its fiscal year ended June 30, 1945, which was claimed as a deduction by Nehi Beverage Company of Hawaii in computing its income tax net income on its return for that fiscal year, which, in turn, was used in computing the net income of petitioner subject to tax for the year 1945;

15. Said sampan was not used by the partnership or others for pleasure purposes during the period it was owned by said Nehi Beverage Company of Hawaii, but was used solely for commercial fishing purposes;

16. That Nehi Beverage Company of Hawaii, a special partnership organized and doing business under the laws of the Terirtory of Hawaii, composed of Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., general partners, and Bishop Trust Company, Limited, a Hawaiian corporation,

Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, special partner, elected to file its tax returns on an accrual and fiscal year basis ending on the 30th day of June of each and every year, and filed its first return on that basis for the fiscal year ended June 30, 1943; that said partnership was dissolved and filed its final return for the fiscal period ending December 10, 1946.

Wherefore Petitioner Prays that this Court may hear the proceeding and determine that there is no deficiency due from the petitioner for the years 1945 and 1946.

/s/ GENEVIEVE H. EATON,
Petitioner.

MILTON CADES,
URBAN E. WILD,
J. RUSSELL CADES,
Counsel for Petitioner.

State of California,
County of Orange—ss.

Genevieve H. Eaton, being duly sworn, says that she is the petitioner above named; that she has read the foregoing petition, or had the same read to her, and is familiar with the statements contained therein; that the statements contained therein are true, except those stated to be upon information and belief, and that those she believes to be true.

/s/ GENEVIEVE H. EATON.

Subscribed and sworn to before me this 5th day of July, 1949.

[Seal] /s/ P. B. HESS,
Notary Public in and for the County of Orange, State of California.

My Commission expires Nov. 14, 1949.

EXHIBIT "A"

Form 1230. SN-IT-1.
IT:FC:LMJ—90D.

Apr. 28, 1949.

Mrs. Genevieve H. Eaton,
Route #1, Box 303,
Fullerton, California.

Dear Madam:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1945, and December 31, 1946, discloses a deficiency of $830.90, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, P. O. Box 421, Honolulu 9, T. H., for the attention of IT:FC:LMJ. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEO. J. SCHOENEMAN,
Commissioner.

By /s/ H. A. PETERSON,
Internal Revenue Agent in
Charge.

Enclosures:
Statement,
Form 1276,
Form of Waiver.

Statement

Mrs. Genevieve H. Eaton
Route #1, Box 303
Fullerton, California

Year	Deficiency
1945	$381.09
1946	449.81
Total	$830.90

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated September 25, 1947, to your protest dated July 14, 1948; and to the statements made at the conference held on March 8, 1949.

A copy of this letter and statement has been mailed to your representative, Mr. Milton Cades, of Smith, Wild, Beebe and Cades, Post Office Box 224, Honolulu, T. H., in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1945

Adjustments to Net Income

Net income as disclosed by return	$8,837.22
Unallowable deductions and additional income:	
(a) Community income	1,029.95
Net income adjusted	$9,867.17

Explanation of Adjustments

(a) Represents your share of additional income of $24,718.75 from the partnership, Nehi Beverage Company of Hawaii, taxable to Mr. Roy Eaton. The amount allocable to you is based on the Hawaii Community Property Law in effect as of June 1, 1945, with the partnership reporting on a fiscal year basis ending June 30, 1945: ½ of 1/12th, or 1/24th of $24,718.75, or $1,029.95.

Computation of Tax

Net income adjusted		$9,867.17
Less: Surtax exemption		500.00
Surtax net income		$9,367.17
Surtax on $9,367.17		$2,424.84
Net income adjusted	$9,867.17	
Less: Normal tax exemption	500.00	
Balance subject to normal tax	$9,367.17	
Normal tax at 3% on $9,367.17		281.02
Correct income tax liability		$2,705.86
Income tax liability disclosed by return, Account No. 300639		2,324.77
Deficiency in income tax		$ 381.09

Taxable Year Ended December 31, 1946

Adjustments to Net Income

Net income as disclosed by return	$27,276.30
Unallowable deductions and additional income:	
(a) Community income	1,552.56
Total	$28,828.86
Nontaxable income and additional deductions:	
(b) Community deductions	621.58
Net income adjusted	$28,207.28

Explanation of Adjustments

(a) Represents one-half of additional income taxable to Mr. Roy Eaton, as follows:

(1) Additional income from the partnership, Nehi Beverage Company of Hawaii, amounting to $446.06: one-half thereof	$ 223.03
(2) Additional net capital gains from the partnership, Nehi Beverage Company of Hawaii, amounting to $1,275.86: one-half thereof	637.93
(3) Additional income from Roy Eaton Trust #1, amounting to $1,383.20: one-half thereof	691.60
Total	$1,552.56

(b) Represents one-half of additional deductions deductible by Mr. Roy Eaton, as follows:

(1) Additional contributions from the partnership, Nehi Beverage Company of Hawaii, amounting to $369.67: one-half thereof	$ 184.83
(2) Additional taxes paid by the partnership, Nehi Beverage Company of Hawaii, and by Roy Eaton Trust #1, amounting to $310.19: one-half thereof	155.10
(3) Trustee's commissions paid by Roy Eaton Trust #1 and #2, amounting to $563.29: one-half thereof	281.65
Total	$ 621.58

Community income and community deductions are allocated to you under the provisions of the Hawaii Community Property Law.

Computation of Alternative Tax

Net income adjusted	$28,207.28
Less: Net long term capital gain	11,783.16
Ordinary net income	$16,424.12
Less: Exemptions	1,000.00
Taxable income	$15,424.12
Combined tentative normal tax and surtax on $15,424.12	$ 4,929.34
Less: 5% of $4,929.34	246.47
Partial tax	$ 4,682.87
Plus: 50% of net capital gain of $11,783.16	5,891.58
Alternative tax	$10,574.45

Computation of Tax

Net income adjusted	$28,207.28
Less: Exemptions	1,000.00
Taxable income	$27,207.28
Combined tentative normal tax and surtax on $27,207.28	$11,488.51
Less: 5% of $11,488.51	574.43
Combined normal tax and surtax	$10,914.08
Correct income tax liability	$10,574.45
Income tax liability disclosed by return, Account No. 300297	10,124.64
Deficiency in income tax	$ 449.81

Received and Filed July 7, 1949, T.C.U.S.

[Title of Tax Court and Cause.]

Docket No. 24082

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I. and II.

Admits the allegations contained in Paragraphs I and II of the petition.

III.

Admits the allegations contained in Paragraph III of the petition, except denies that the entire amount of the deficiencies is in controversy.

IV.

1 to 9, inclusive. Denies that the Commissioner erred in the determination of the deficiency as alleged in Paragraph IV of the petition and Subparagraphs 1 to 9, inclusive, thereunder.

V.

1. Admits that Roy Eaton, the husband of petitioner, on September 30, 1942, settled Trust No. 1, by a transfer to Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, of a sum of Fifteen Thousand

Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 1 of Paragraph V of the petition.

2. Admits that by the terms of said Trust Agreement, the Trustee was to contribute the said sum of Fifteen Thousand Dollars ($15,000.00) to the capital of Nehi Beverage Company of Hawaii; denies the remaining allegations contained in Subparagraph 2 of Paragraph V of the petition.

3. Admits the allegations contained in Subparagraph 3 of Paragraph V of the petition.

4 and 5. Denies the allegations contained in Subparagraphs 4 and 5 of Paragraph V of the petition.

6. Admits that the gross income reported by Trust No. 1, for the taxable year 1946, included an item designated investment income in the amount of $1,383.20; denies the remaining allegations contained in Subparagraph 6 of Paragraph V of the petition.

7. Admits that the said Roy Eaton, on February 28, 1943, settled Trust No. 2 by a transfer to said Bishop Trust Company, Limited, as Trustee, of a sum of Fifteen Thousand Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 7 of Paragraph V of the petition.

8. Admits that by the terms of said Trust Agreement, a thirty per cent (30%) capital interest in

Nehi Beverage Company of Hawaii was to be acquired for Fifteen Thousand Dollars ($15,000.00); denies the remaining allegations contained in Subparagraph 8 of Paragraph V of the petition.

9. Admits that under the terms of said Trust Agreement the Trustee was required to accumulate all income until the youngest of the children of the Settlor reached the aged of twenty-five (25) years, without any discretion to distribute any portion of the income or principal for the support, maintenance and education of the beneficiaries; denies the remaining allegations contained in Subparagraph 9 of Paragraph V of the petition.

10. Admits that as of February 28, 1943, Trust No. 2 purchased from Trust No. 1 its interest as an alleged special partner in said Nehi Beverage Company of Hawaii; denies the remaining allegations contained in Subparagraph 10 of Paragraph V of the petition.

11. Admits that the gross income reported by Trust No. 2, for the taxable year 1945, included an item designated as income from said partnership in the amount of $23,714.38; denies the remaining allegations contained in Subparagraph 11 of Paragraph V of the petition.

12. Admits that the gross income reported by Trust No. 2, for the taxable year 1946, included an item designated as income from said partnership in the amount of $446.06, and a net capital gain of said partnership in the amount of $1,275.86; denies

the remaining allegations contained in Subparagraph 12 of Paragraph V of the petition.

13. Admits that Nehi Beverage Company of Hawaii purchased a sampan; denies the remaining allegations contained in Subparagraph 13 of Paragraph V of the petition.

14. Admits that Nehi Beverage Company of Hawaii claimed a deduction of $1,004.37 in computing its income tax net income on its return for the fiscal year ended June 30, 1945, which, in turn, was used in computing the net income of petitioner subject to tax for the year 1945; denies the remaining allegations contained in Subparagraph 14 of Paragraph V of the petition.

15. Denies the allegations contained in Subparagraph 15 of Paragraph V of the petition.

16. Admits that Nehi Beverage Company of Hawaii filed a return for the fiscal year ended June 30, 1943, and filed its final return for the fiscal period ending December 10, 1946; denies the remaining allegations contained in Subparagraph 16 of Paragraph V of the petition.

VI.

Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's

determination be approved and the petitioner's appeal denied.

/s/ CHARLES OLIPHANT,
Chief Counsel, Bureau of
Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel;

T. M. MATHER,
LEONARD A. MARCUSSEN,
Special Attorneys, Bureau of
Internal Revenue.

Received and filed August 24, 1949, T.C.U.S.

The Tax Court of the United States

Docket No. 24081

ROY EATON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 24082

GENEVIEVE EATON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STIPULATION OF FACTS

It Is Hereby Stipulated and Agreed, by and between the parties hereto, by their respective attor-

neys, that the following facts shall be taken as true and may be received by the Court in evidence with the same force and effect as if the facts herein contained were testified to by competent witnesses; Provided, However, that this stipulation shall be without prejudice to the right of either party to introduce other or further evidence not inconsistent with the facts herein stipulated as true:

I.

That petitioners Roy Eaton and Genevieve Eaton are, and were at all times material to this proceeding, husband and wife and residents of the Territory of Hawaii or Fullerton, California.

II.

That petitioners have three children, Ann Eaton Weaver (Mrs. Neal F. Weaver), born April 17, 1930; Peter Eaton, born February 20, 1932, and Timothy Eaton, born August 28, 1934.

III.

That petitioner Roy Eaton, in May, June and July, 1942, had correspondence by mail with Nehi Corporation with respect to franchises he held for Nehi, Par-T-Pak and Royal Crown Cola for the Territory of Hawaii. True copies of letters from petitioner Roy Eaton to Nehi Corporation dated May 21, 1942; from Nehi Corporation to petitioner Roy Eaton dated June 3, 1942; from petitioner Roy Eaton to Nehi Corporation dated July 7, 1942, and from Nehi Corporation to petitioner Roy Eaton

dated July 14, 1942, marked Exhibits 1, 2, 3 and 4, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

IV.

That petitioner Roy Eaton, on September 30, 1942, settled a trust, hereinafter referred to as "Trust No. 1," by a transfer to Bishop Trust Company, Limited, a corporation organized under the laws of the Territory of Hawaii, of the sum of $15,000.00, in conformity with that certain Indenture dated the 30th day of September, 1942, a true copy of which, marked Exhibit 5, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

V.

That a Special Partnership Agreement, dated the 30th day of September, 1942, was duly executed by Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942. A true copy of said Special Partnership Agreement, marked Exhibit 6, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VI.

That a Bill of Sale, dated as of the close of business on September 30, 1942, was duly executed by Roy Eaton, as Seller, and Nehi Beverage Company of Hawaii, a Special Partnership. A true

copy of said Bill of Sale, marked Exhibit 7, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VII.

That on November 2, 1942, a duly executed Certificate of Special Partnership, together with Affidavits of Roy Eaton, Charles P. Johnson, Walter L. Prock, Jr., and W. A. White, required by Section 6875, Revised Laws of Hawaii, 1935, were duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii, 1935. A true copy of said Certificate and Affidavits, marked Exhibit 8, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

VIII.

That a Statement of the Substance of Certificate of Special Partnership was duly published in The Honolulu Advertiser on November 9, 10, 16 and 17, 1942.

IX.

That petitioner, on February 28, 1943, settled a trust, hereinafter referred to as "Trust No. 2," by a transfer to said Bishop Trust Company, Limited, of a sum of $15,000.00, in conformity with that certain Indenture dated the 28th day of February, 1943, a true copy of which, marked Exhibit 9, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

X.

That on February 28, 1943, Trust No. 2 purchased from Trust No. 1 all of its right, title and interest in and to its 30% capital interest in the Special Partnership known as "Nehi Beverage Company of Hawaii," which was duly assigned to said Trust No. 2 by Assignment dated the 28th day of February, 1943. A true copy of said Assignment, marked Exhibit 10, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XI.

That Trust No. 1 loaned the sum of $15,000.00 to Nehi Beverage Company of Hawaii on February 28, 1943, receiving a note due one year after demand therefor with interest at 5% per annum. Interest was paid periodically and said note was repaid in full on November 23, 1946.

XII.

That an Amendment of Special Partnership Agreement, dated the 28th day of February, 1943, was duly executed by Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943. A true copy of said Amendment of Special Partnership Agreement, marked Exhibit 11, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIII.

That on April 26, 1943, a duly executed Certifi-

cate of Change of Special Partnership and Affidavits of Roy Eaton, Charles P. Johnson, Walter L. Prock, Jr., and W. A. White, required by Section 6875, Revised Laws of Hawaii, 1935, were duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii, 1935. A true copy of said Certificate and Affidavits, marked Exhibit 12, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIV.

That a Statement of Substance of Certificate of Change of Special Partnership was duly published in The Honolulu Advertiser on May 3, 4, 10 and 11, 1943.

XV.

That on June 30, 1946, petitioner Roy Eaton purchased from Charles P. Johnson and Walter L. Prock, Jr., all of their interest in Nehi Beverage Company of Hawaii, and a Bill of Sale, dated as of the close of business on June 30, 1946, was duly executed by Charles P. Johnson and Walter L. Prock, Jr., as Sellers, and Roy Eaton, as Purchaser. A true copy of said Bill of Sale, marked Exhibit 13, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XVI.

That on September 12, 1946, a Certificate of Change of Special Partnership was duly filed in the Office of the Treasurer of the Territory of Hawaii

in accordance with the provisions of Chapter 225, Revised Laws of Hawaii, 1935. A true copy of said Certificate, marked Exhibit 14, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XVII.

That a Statement of Substance of Certificate of Change of Special Partnership was duly published in The Honolulu Advertiser on September 16, 19, 23 and 26, 1946.

XVIII.

That Nehi Beverage Company of Hawaii sold all of its assets and property to Nehi Beverage Company of Hawaii, Limited, as of the opening of business on October 1, 1946. A true copy of the confirmation letter of agreement, dated October 11, 1946, signed by the parties thereto, marked Exhibit 15; a true copy of Bill of Sale duly executed by the parties thereto, marked Exhibit 16; a true copy of Assignment of Lease duly executed by the parties thereto, marked Exhibit 17; true copies of duly executed notes of Nehi Beverage Company of Hawaii, Limited, to Roy Eaton, in the amounts of $91,000.00 and $24,500.00, and to Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, Settlor, in the amounts of $39,000.00 and $10,500.00, marked Exhibits 18, 19, 20 and 21, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XIX.

That on December 10, 1946, Cancellation of Certificate of Special Partnership of Nehi Beverage Company of Hawaii was duly filed in the Office of the Treasurer of the Territory of Hawaii in accordance with the provisions of Chapter 225, Revised Laws of Hawaii, 1935. A true copy of said Cancellation, marked Exhibit 22, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XX.

That a Notice of Dissolution of Special Partnership was duly published in the Honolulu Star-Bulletin on December 16, 23 and 30, 1946, and January 6, 1947.

XXI.

That Nehi Beverage Company of Hawaii duly elected to file its partnership tax returns on an accrual and fiscal year basis ending on the 28th of February, and filed its first return on that basis for the fiscal year ended February 28, 1943. A photostatic copy of said return, marked Exhibit 23, is attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXII.

That after the withdrawal of Trust No. 1 and the admission of Trust No. 2, Nehi Beverage Company of Hawaii elected to file its partnership tax returns on an accrual and fiscal year basis ending on the 30th day of June, and filed its first return on that

basis for the fiscal year ended June 30, 1943. After dissolution of the Special Partnership, Nehi Beverage Company of Hawaii filed its final return for the fiscal year ended December 10, 1946. Photostatic copies of the returns filed by Nehi Beverage Company of Hawaii for the fiscal periods ended June 30, 1943; June 30, 1944; June 30, 1945; June 30, 1946, and December 10, 1946, marked Exhibits 24, 25, 26, 27 and 28, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXIII.

That Schedules showing the income and expenses for the period from September 30, 1942, to September 30, 1950, the payments received as distributions of its share of income of Nehi Beverage Company of Hawaii, and the inventories of assets of Trust No. 1 at September 30, 1950, as shown by the books and records of said Trust, marked Exhibits 29, 30* and 31, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXIV.

That Schedules showing the income and expenses for the period from February 28, 1943, to February 28, 1951, the payments received as distributions of its share of income of Nehi Beverage Company of Hawaii, and the inventories of assets of Trust No.

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*By agreement of the parties, Exhibit 30 is omitted.

2 at February 28, 1951, as shown by the books and records of said Trust, marked Exhibits 32, 33 and 34, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXV.

That Trust No. 1 and Trust No. 2 duly filed federal fiduciary returns each year and duly paid the tax shown to be due thereon. Schedules showing the items of income and deductions shown on said tax returns of Trust No. 1 and Trust No. 2, marked Exhibits 35 and 36, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes. Photostatic copies of the fiduciary tax returns filed by said Trust No. 1 for the years 1943, 1944, 1945 and 1946, marked Exhibits 37, 38, and 39 and 40, respectively, and by said Trust No. 2 for the same years, marked Exhibits 41, 42, 43 and 44, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXVI.

That a photostatic copy of the joint tax return filed by petitioners for the year 1942, photostatic copies of the tax returns of petitioner Roy Eaton for the years 1943, 1944, 1945 and 1946, and of petitioner Genevieve Eaton for the years 1945 and 1946, marked Exhibits 45, 46, 47, 48, 49, 50 and 51, respectively, are attached hereto, incorporated herein by reference, and made a part hereof for all purposes.

XXVII.

That in the deficiency notice addressed to petitioner Roy Eaton, respondent increased income from the partnership, Nehi Beverage Company of Hawaii, by the disallowance of net sampan operating losses in the amounts of $5,509.08 and $1,104.37 for the years 1944 and 1945, respectively. It Is Hereby Stipulated and Agreed that said deductions are allowable deductions from total partnership income for said years, And It Is Further Agreed that a net capital gain of $392.00 on the sale of said sampan in 1945, which was reported on the partnership return of said partnership for the fiscal year ended June 30, 1945, is properly includable in the income of said partnership for said fiscal year.

XXVIII.

That by virtue of the Hawaiian Community Property Law, which became effective as of June 1, 1945, petitioner Genevieve Eaton was entitled to one-half of all of the income of her husband, petitioner Roy Eaton, from and after that date.

XXX.

That the entire amount of the deficiency asserted against petitioner Genevieve Eaton arises by reason of her community property interest in the income of her said husband, petitioner Roy Eaton.

/s/ MILTON CADES,
Counsel for Petitioners.

/s/ CHARLES OLIPHANT, CWN
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

EXHIBIT No. 1

May 21, 1942.

Via Clipper.
Nehi Corporation,
Columbus, Georgia.

Attention: Mr. C. C. Colbert.

Gentlemen:

As the holder of your franchises throughout the Territory of Hawaii for Nehi, Par-T-Pak and Royal Crown, which franchises are entirely personal to me, I am somewhat exercised, in view of current conditions, concerning the manner in which I may be able to guarantee the future of my wife and children in the event I should die. As you know, I hold valuable leaseholds and have a very considerable investment in equipment for the bottling and distribution of Nehi products locally. In fact I have put "my all" into this Nehi plant and am devoting my entire time and efforts in promoting Nehi products here in the Territory of Hawaii. It is only natural that in the event of my death I would want the business to continue without interruption and the benefits of this my principal asset to accrue to my wife and children.

You have no doubt encountered similar situations many times in the past and must have some ideas as to how my situation could be satisfactorily handled under the terms of your franchises.

May I hope to have your advice in this regard at your earliest convenience?

Sincerely,

ROY EATON.

EXHIBIT No. 2

Nehi Corporation
Columbus, Georgia

June 3, 1942.

Mr. Roy Eaton,
Nehi Beverage Company of Hawaii,
Kona and Hopaka Streets,
Honolulu, Hawaii.

Dear Mr. Eaton:

It was very gratifying to receive your communication of May 21. Of course we have heard from you through George Silver, ever since he finally succeeded in making his first contact, after December 7, 1941.

Aside from the question discussed in your letter of the 21st, I hope that all other matters pertaining to your operations are getting along as well as could be expected under existing circumstances.

Your question of course is one which is the same for every person who obtains our franchises or others of a similar nature. I judge that the question is one of protecting for your own family valuations that you have built up yourself, which you fear might to some extent be dissipated or depreciated in the case of your own untimely death.

Our franchises are personal contracts issued to individuals. They are not transferable without our consent nor are they inheritable. However, it is and always has been our policy to deal in the utmost fairness with our bottlers and we are not unaware of their efforts and investments. When a bottler

meets an untimely death you may be sure it is our desire to conserve for his family all that we can and to follow so far as possible the wishes of his family with respect to operation or disposal of the business.

Now, I know, I am asking you to rely on faith and not on contractual obligation. However, I must do that since we cannot in advance agree to future transfers of franchises. I am sure you need have no concern upon this subject since I know the policy of our Company and its interest in the welfare of its bottlers and their families.

I believe you will agree that all of our bottlers must in large degree rely upon the good faith of our Company. In our franchises we reserve the right of cancellation but never have we exercised that right for the purpose of diminishing values nor unless the circumstances compelled cancellation.

After reading the foregoing, I shall be glad to hear from you further, with any suggestion that you yourself might have in the matter.

With best wishes, I am,

Yours sincerely,

/s/ C. C. COLBERT,
President.

CCC:LLJ.

EXHIBIT No. 3

Via Clipper.

July 7, 1942.

Mr. C. C. Colbert,
Nehi Corporation,
Columbus, Georgia.

Dear Mr. Colbert:

Thank you very much for your prompt reply to my letter of May 21. I am happy to report that our operations are getting along very well under the existing circumstances.

As Mr. Silver has no doubt told you we are not hampered by sugar quotas. However the new crown rationing order could prove very difficult because of the length of time between the placing of an order and receipt of crowns. I understand that the Crown Cork and Seal Company is making every effort to secure some exceptions to the order as it pertains to Hawaii. They were successful in having the time limit extended under the former order and I am very hopeful that they will succeed again.

If the crown manufacturers will give us seventy per cent of last years sales plus the amount needed by military posts which I understand is the present plan, the limitations on use will not materially affect us because such a large percentage of our business is with government agencies.

We are having plenty of trouble obtaining adequate labor and other difficulties, but I am sure they are not worse than other businesses are faced with everywhere and I am very grateful that we are

getting along as well as we are. George Silver has been most cooperative and helpful and it is really a great comfort to have such a fine organization as Nehi backing us up.

Regarding the working out of some plan for the protection of the business and my family if something should happen to me, it is difficult for me to know what to suggest not being familiar with your practices under those circumstances.

On the mainland I would imagine your district manager or one of his assistants would be available to do what was necessary in supervising continued purchases and use of concentrate and crowns, etc., until a definite settlement has been made. He could determine whether the plant personnel was adequate to carry on and if a sale was involved represent Nehi Corporation in such a transaction.

Over here all this would be impossible. Under present circumstances it would probably be a matter of months before anyone could get here and even longer before they could return. Territorial laws governing inheritance, particularly where children are involved would further complicate matters.

The loss which would be sustained by Nehi Corporation as well as my estate in case it was not possible to continue operations for even a brief period would be considerable. I do not question the fact that Nehi Corporation would be fair in dealing with my estate. However, based on ten years experience as an executive of California's largest Memorial Park, I know that untold loss to say nothing of inconvenience and grief could be prevented if

proper arrangements were made regarding the disposition of estates before death occurs. Making such arrangements under existing conditions is even more important than during normal times.

Until the matter can be gone into more thoroughly I would very much appreciate a letter stating in detail just what procedure you would want the executors of my estate to follow to insure the continuance of the business until arrangements could be made to have the franchise placed in another name.

Sincerely yours,

ROY EATON.

RE:rh.

EXHIBIT No. 4

Nehi Corporation
Columbus, Georgia

July 14, 1942.

Mr. Roy Eaton,
Nehi Beverage Company,
Kona and Hopaka Streets,
Honolulu, Hawaii.

Dear Mr. Eaton:

I have your interesting letter of July 7, and the information contained in it is very heartening. We regret that we have been in no better position to help you under the existing circumstances.

Undoubtedly the efforts the Crown Cork & Seal Company is making is the best course that can be pursued in the matter of your crown supply. They

did get permission to ship our bottler at San Juan, Puerto Rico a larger supply of crowns than the 20% inventory provision in the crown order, with the agreement that they would of course be used only in accordance with the order. We will see if our Washington representative can be of any assistance in this matter with respect to your supply.

It seems to us that if in your will you were to authorize and instruct your executors to continue the operation of the plant until a sale could be made suitable to them and to Nehi Corporation, or until such other time as would be agreed upon between your executors and Nehi Corporation, that would be about as much insurance as you could provide for adequate continuance.

You will of course have selected executors in whom you have complete confidence as to integrity and judgment, and you undoubtedly have confidence in the integrity of Nehi Corporation, or you would not have made the large investment you did in connection with your relationship here.

Therefore, if you place your executors in the position of exercising discretion and using their judgment in the matter of continuing the business in collaboration with the judgment of Nehi Corporation management, you will have left the matter in the best possible shape in our opinion.

If there is any further thought that we may have in this connection, and in respect to which it may seem advisable to go more into detail with, our Vice President and General Counsel, Mr. Willis Battle, will write you.

Again I say it was very thoughtful of you to write so clearly about the situation over there, and while we know George Silver has been keeping in continuously close contact with you, as close as possible, we are happy always to have this kind of advice directly as well.

With kindest regards and best wishes, we are

Yours sincerely,

NEHI CORPORATION.

/s/ C. C. COLBERT,
President.

CCC:BB.

P.S. If there is anything we can do about the crown matter, you will hear from us as soon as possible.

C.C.C.

EXHIBIT No. 5

This Indenture, dated this 30th day of September, 1942, by and between Roy Eaton, of Honolulu, City and County of Honolulu, Territory of Hawaii, a citizen of the United States of America, hereinafter called the "Settlor," and Bishop Trust Company, Limited (a corporation duly organized and existing under the laws of the Territory of Hawaii and a majority of whose officers and directors are citizens of the United States of America), hereinafter called the "Trustee,"

Exhibit No. 5—(Continued)

Witnesseth That:

The Settlor, in consideration of the love and affection he bears the beneficiaries and of the acceptance by the Trustee of the trust herein created, does hereby transfer, set over and deliver to the Trustee, its successors in trust and assigns, the sum of Fifteen Thousand and no/100ths Dollars ($15,000.00);

To Have and to Hold the same, together with all other property which may hereafter be or become a part of the trust estate hereby created, unto the Trustee, its successors in trust and assigns, in trust nevertheless for the uses and purposes hereinafter stated, that is to say:

(a) The Trustee shall contribute the sum of Fifteen Thousand and no/100ths Dollars ($15,000.00) to the capital of the partnership known as Nehi Beverage Company of Hawaii, a partnership duly organized and operating under that certain Special Partnership Agreement dated September 30, 1942, for a thirty per cent (30%) interest therein, and continue to be a special partner in such partnership, said sum being the fair and reasonable value of said interest duly ascertained as of September 30, 1942;

(b) The Trustee shall accumulate all net income from the said trust estate during the continuation of this trust; Provided, However, that the Trustee during such time may in its sole discretion pay out of the net income of the said trust estate to or apply for the use and benefit of any of the children of the Settlor or the lawful issue of any of them who shall

Exhibit No. 5—(Continued)

die during the continuance of this trust, such amounts as may be necessary for their maintenance, support and education; Provided, Further, that the Trustee shall not in any year pay out or apply or use for the benefit of the issue of any deceased child of the Settlor more than one-third (⅓) of the net income of the said trust estate for such year; and all income not so distributed in any calendar year shall, at the end of such year, be added to and become a part of the corpus of the trust estate;

(c) The Trustee is hereby authorized and empowered to pay from the corpus of the said trust estate any sum or sums from time to time and for such periods of time as in its sole discretion it shall deem necessary or proper for the support, maintenance and education of any of the children of the Settlor whenever the Trustee in its sole discretion deems the income which any of them is receiving insufficient for such purposes; and such payment shall not be deemed an advancement of corpus to any child, and the Trustee shall be under no obligation in such use of corpus to pay or use corpus equally or proportionately for said children, and all payments from the corpus of the trust estate shall be binding upon all beneficiaries hereunder;

(d) This trust shall cease and determine when the youngest of the children of the Settlor, who shall continue to survive, shall have attained the age of twenty-five (25) years, or upon the prior death of the last survivor of the said children and the property comprising the said trust estate, to-

Exhibit No. 5—(Continued)

gether with the accumulated income thereof, shall at such time vest in and be transferred, conveyed and delivered by the Trustee absolutely and in fee simple, free and clear from any trusts, in equal shares to those who are surviving of the children of the Settlor, and the lawful issue of any of said children who shall then be dead, said issue to take per stirpes and not per capita; and in the event that this trust shall have ceased and determined upon the death of the last survivor of the children of the Settlor, and no lawful issue of said children shall be then surviving, then the said property and income shall at such time vest in and be transferred, conveyed and delivered by the Trustee absolutely and in fee simple to those persons other than the Settlor who would be the heirs-at-law of the last survivor of the children of the Settlor under the statutes of descent of the Territory of Hawaii in force and effect at the time of his or her death, the same as if he or she had died intestate at that time; Provided, However, that in the event that the partnership known as "Nehi Beverage Company of Hawaii" shall terminate during the continuance of this trust, the Trustee may determine this trust at any time thereafter which to the Trustee may seem best, and thereupon the property comprising the said trust estate, together with the accumulated income thereof, shall vest in and be transferred, conveyed and delivered by the Trustee, absolutely and in fee simple, free and clear from any trusts, in equal shares to those who are surviving of the chil-

Exhibit No. 5—(Continued)

dren of the Settlor and the lawful issue of any of said children who shall then be dead, said issue to take per stirpes and not per capita;

(e) The Trustee shall receive, hold, manage and control the said trust estate, collect the income therefrom and pay all charges incident to trust estates and properly payable by said trust estate therefrom; and the Settlor authorizes the Trustee to retain either permanently or temporarily or for such period of time as it may deem expedient any property conveyed, assigned or delivered to the Trustee by the Settlor of whatever nature; and the Settlor directs that the said Trustee shall not be held liable for any loss resulting to said trust estate by reason of the Trustee's retaining any such property or for any error of judgment in this respect;

(f) The Settlor authorizes and empowers the Trustee to sell at public or private sale, convert, transfer, exchange, mortgage, hypothecate and otherwise deal in or dispose of the whole or any part of the property, real, personal or mixed, which may be from time to time a part of the trust estate, with power to accept any purchase money mortgage or mortgages for any part of the purchase or exchange price; to invest and reinvest the whole or any part of the assets of the said trust estate, and in investing and reinvesting any assets of said trust estate the Trustee may invest in common or preferred stocks of corporations, bonds, notes, debentures, participation or investment certificates and/or in any other property, real or personal, in so far as in

Exhibit No. 5—(Continued)

its judgment it shall deem such investments advisable, it being the intention of the Settlor, under the foregoing provisions, to grant to the Trustee full power to invest and reinvest money in such investments as it shall deem desirable and suitable investments for trust funds without being restricted to the classes of investments which trustees are permitted by law to make, provided, however, that the Trustee shall obtain the consent of the Settlor to make such investments during his lifetime, and provided further that in the event the Settlor shall die before the termination hereof, the Trustee shall thereafter be restricted in the making of investments of trust funds to the classes of investments which trustees are permitted by law to make, except that in any event the Trustee may, without liability for any losses resulting therefrom, make advances or loans to or other or further investments in the partnership known as "Nehi Beverage Company of Hawaii"; the Settlor authorizes and empowers the Trustee, upon any increase of the capital stock of any corporation in which said trust estate shall own shares, to exercise any preemptive rights to such shares to which said trust estate may be liable and/or to subscribe for such additional shares as in the judgment of the Trustee shall be an advisable investment; and for this purpose and for other purposes of this trust, the Settlor authorizes and empowers the Trustee to borrow money either from itself or from others and upon such terms and conditions as it may deem appropriate; the Trustee

Exhibit No. 5—(Continued)

shall have the right and power to vote either directly or by proxy the stock of any corporation that may be a part of said trust estate from time to time at all meetings of stockholders as the Trustee may deem best;

(g) Stock dividends shall be treated as capital of the trust estate and all stock acquired by the Trustee under the exercise of rights to subscribe or the net proceeds realized by the Trustee from the sale of rights to subscribe shall be treated as capital of the trust estate and all other corporate distributions shall be treated as income; provided, however, that where a distribution is made through the reduction of any corporate stock held by the Trustee, or, in the exclusive discretion of the Trustee it appears to be made in or as a result of a partial or complete liquidation or dissolution of the corporation, the Trustee may in its discretion make such apportionment of any such distribution between income and capital as to it may seem just; the Trustee shall have full power and authority to decide and determine in all doubtful cases what property or moneys received by it is capital and what is income; and also in all doubtful cases to decide and determine what expenses and other charges are payable out of income and what out of capital; and also in all doubtful cases to decide and determine what proportion of payments for expenses of or charges against the trust estate are payable from income and what from capital; and all beneficiaries shall be bound by the decision and determination of the

Exhibit No. 5—(Continued)

Trustee in regard to all such allocations between capital and income; the Trustee shall have authority in and discretion to prorate during the year and withhold from the income received by the trust estate an amount sufficient to pay proportionate shares of the expenses payable by the trust estate so that said payments of net income may be more regular and even in amount, and to withhold such amounts of income and/or principal as it may deem necessary to protect itself from any possible liability for taxes and/or costs or expenses in connection with or arising out of possible claims therefor;

(h) The Settlor may transfer, convey and assign to the Trustee any property in addition to that hereinbefore referred to, to be held upon the trust hereby created, and thereafter such additional property shall be and form a part of the trust estate;

(i) The Trustee shall render annual statements of account to the persons who are the beneficiaries of this trust, as hereinabove provided, but the Trustee shall not be required to account in any court unless requested so to do by a beneficiary; Provided, However, that the Trustee may whenever it shall deem it advisable file accounts in any court having jurisdiction thereof for approval, the costs of said proceeding to be paid out of the trust estate;

(j) If any person entitled to receive any of the income and/or corpus of the trust estate shall be a minor, the Trustee may pay the share of income and/or corpus to which said minor is entitled to

Exhibit No. 5—(Continued)

either parent or to the natural or legally appointed guardian of such minor, for the account, benefit or use of such minor, and the receipt of such parent or natural or legally appointed guardian shall be a complete release, discharge and acquittance of the Trustee to account further for any payment or payments so made, and if any beneficiary is a minor, the statements of account may be furnished to either parent or to the natural or legally appointed guardian of such minor beneficiary;

(k) The Trustee shall have the custody and safekeeping of all moneys and securities belonging to the trust estate which are received or collected by the Trustee. The Trustee may rely upon auditor's reports of the business of the partnership known as "Nehi Beverage Company of Hawaii," and shall not be required to make any independent investigation into its affairs or accounts, and the Trustee shall not be answerable or accountable for any loss or damage resulting from any error of judgment or otherwise except through its own gross negligence or wilful default, nor shall the Trustee be answerable or accountable for any loss or damage resulting from any act consented to by the Settlor or for any loss or damage resulting from any investment in or loan or advance to the partnership known as "Nehi Beverage Company of Hawaii";

(l) No beneficiary hereunder shall have the power or authority to anticipate in anywise any of the rents, issues, profits, income, moneys or payments herein provided to be devoted or paid to him

Exhibit No. 5—(Continued)

or her or any part thereof, nor to alienate, encumber, convey, transfer or dispose of the same or of any interest therein or part thereof, in advance of payment; nor shall the same be involuntarily alienated by him or her or be subject to attachment or execution or be levied upon or taken upon any process for any debts which any such beneficiary shall have contracted or in satisfaction of any demands or obligations which he or she shall incur. All payments or distribution of either income and/or principal as hereinabove provided shall be made by the Trustee and subject to the provisions of subparagraph (j) hereinabove shall be valid and effectual only when made to the beneficiary to whom the same shall appertain and belong, and upon his or her individual receipt; Provided, However, that when and while the person so entitled to receive such payment shall be without the bounds of the Territory of Hawaii, such payment may be made to any formally appointed agent of such person, but only upon the personal receipt above provided for;

(m) It is hereby declared that this agreement shall be and is hereby made irrevocable by the Settlor and the Settlor reserves the right to amend this instrument only by adding other property to be and become a part of the estate held under the terms hereof, and the right to alter, amend, cancel or revoke any provisions of this instrument, save and except paragraphs (a), (b), (c) and (d) hereof; Provided, However, that in no event shall any of

Exhibit No. 5—(Continued)

the property or the income thereof belonging to the trust estate be paid to or inure to the benefit of the Settlor, and Provided Further, that any amendments made by the Settlor shall be made by instrument in writing and acknowledged and filed with the Trustee, and that the alteration, amendment, cancellation or revocation of any provision of this instrument shall be made only with the written consent and approval of the Trustee;

The said Bishop Trust Company, Limited, hereby accepts the within trust and covenants and agrees with the Settlor that it will faithfully discharge and carry out the same.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

/s/ ROY EATON,
Settlor.

[Seal] BISHOP TRUST COMPANY, LIMITED,

By /s/ W. A. WHITE,
Its Vice President;

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres. Trustee.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Roy Eaton, to me known to be the

Exhibit No. 5—(Continued)

person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 31st day of October, 1942, before me appeared W. A. White and E. Benner, Jr., to me personally known, who being by me duly sworn, did say that they are Vice President and Asst. Vice President, respectively, of Bishop Trust Company, Limited, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ THEODORA B. TOWNSEND,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

EXHIBIT No. 6

This Special Partnership Agreement, dated this 30th day of September, 1942, by and between Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., all of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter referred to as "General Partners," and Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, hereinafter referred to as the "Special Partner,"

Witnesseth That:

Whereas, the parties hereto having mutual confidence in each other, do hereby form with each other a Special Partnership for the purpose of acquiring and thereafter carrying on the business heretofore carried on by Roy Eaton and known as "Nehi Beverage Company of Hawaii," from and after the close of business on September 30, 1942, and for other purposes as hereinafter provided upon the following terms and conditions, that is to say:

1. Purposes. The purposes of the partnership shall be to acquire as at the close of business on September 30, 1942, all assets and to carry on the business heretofore carried on and conducted by Roy Eaton under the name of "Nehi Beverage Company of Hawaii"; to buy, sell, import, export, bottle, manufacture, trade and deal in beverages, extracts, syrups and goods, wares and merchandise of every kind and nature and to engage in and carry on the business of general wholesale and re-

Exhibit No. 6—(Continued)

tail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers; to buy or otherwise acquire or hold, use, improve, develop, mortgage, lease or take on lease, sell, convey and in any and every other manner deal in and with and dispose of real estate, buildings and other improvements, hereditaments, easements and appurtenances of every kind in connection therewith, or any estate or interest therein of any tenure or description, to the fullest extent permitted by law and also any and all kinds of chattels, goods, wares, merchandise and agricultural, manufacturing and mercantile products and commodities and patents, licenses, debentures, securities, stocks, bonds, commercial paper and other forms of assets, rights and interests and evidences of property or indebtedness, tangible or intangible; to undertake and carry on any business investment, transaction, venture or enterprise which may lawfully be undertaken or carried on by a partnership, and any business whatsoever that may seem to the partnership convenient or suitable to be undertaken whereby, directly or indirectly, to promote any of its general purposes or interests or render more valuable or profitable any of its property, rights, interests or enterprises; and to acquire by purchase, lease or otherwise, the property, rights, franchises, assets, business and good will of any person, firm, association or corporation engaged in or authorized to conduct any business or undertaking which may be carried on by this partnership or possessed of any

Exhibit No. 6—(Continued)

property suitable or useful for any of its own purposes, and carry on the same; and undertake all or any part of the obligations and liabilities in connection therewith on such terms and conditions and for such consideration as may be agreed upon; and to pay for the same either all or partly in cash, stocks, bonds, debentures or other forms of assets or securities; and to effect any such acquisition or carry on any business authorized by this Agreement, either by directly engaging therein, or indirectly by acquiring the shares, stocks or other securities of such other business or entity and holding and voting the same and otherwise exercising and enjoying the rights and advantages incident thereto; and such other business as may be necessary, suitable or proper to the accomplishment of their purposes or connected or related thereto as the partners from time to time mutually may agree.

2. Name. The partnership shall be conducted and carried on under the same name and style of Nehi Beverage Company of Hawaii, and the place or places of business shall be at Honolulu aforesaid, and/or at such other place or places as the partners may from time to time determine.

3. Capital. The capital of the partnership as of the date of commencement of the term provided for by this Agreement, shall be the sum of $50,000.00, which amount is the cost of the net assets acquired by the partnership as of September 30, 1942, and it is agreed that the contributions of capital of each

Exhibit No. 6—(Continued)

of the partners to the Agreement shall be as follows:

	Amount	Interest & Percentage
Roy Eaton	$30,000.00	60%
Charles P. Johnson	2,500.00	5%
Walter L. Prock, Jr. ...	2,500.00	5%
Bishop Trust Co., Ltd., Trustee under Deed of Trust of Roy Eaton, dated Sept. 30, 1942...	15,000.00	30%
	$50,000.00	100%

It Is Understood and Agreed that Bishop Trust Company, Limited, Trustee as aforesaid, shall be a Special Partner in its capacity as Trustee and not individually and shall have all the powers, rights and duties of a Special Partner as prescribed by Chapter 225 of the Revised Laws of Hawaii, 1935, as the same now is or as the same may from time to time be amended, and that the Special Partner shall not be liable for the debts of the partnership to any extent beyond that set forth in the provisions of Section 6887 of the Revised Laws of Hawaii, 1935, as the same now is or as the same may from time to time to amended.

4. Compensation of General Partners and Division of Profits. From time to time, and as the General Partners may agree, the General Partners

Exhibit No. 6—(Continued)

actively engaged in the business of the partnership shall receive, as compensation for services rendered to the partnership, a salary chargeable for purposes of computing net profits hereunder, as an expense of the business, in such amount as the General Partner or Partners owning the majority in interest of the capital contributed by the General Partners, may from time to time agree upon, constituting the reasonable value of the services rendered to the partnership. All of the remaining net profits of the partnership shall be divided for each annual period in proportion to the above-stated interest of each of the partners in the original capital of the partnership, and all losses of the partnership for each annual period shall be divided among the partners in the same manner as herein provided for the division of profits; Provided, However, that General Partners Charles P. Johnson and/or Walter L. Prock, Jr., shall only be entitled to such amount of the net profits of the business during any period of time in which the business of the partnership is not the principal activity of said partner, as is not in excess of 12% per annum of the amount of said General Partner's capital interest, and the remaining net profits of the partnership shall be divided in proportion to the above-stated interest of each of the other partners in the original capital of the partnership. Any partner may withdraw from the partnership such portion of the profits attributable to said partner's interest as the General Partners may from time to time deem advisable. Amounts

Exhibit No. 6—(Continued)

not withdrawn shall not be added to the capital account but shall be credited to advance accounts in the names of the respective partners for whom said amounts are being held, and no interest shall be paid on said accounts.

5. Services of the Partners. The General Partners shall diligently give as much of their time, attention and services to the business of the partnership as the General Partner or Partners owning the majority in interest of the capital contributed by the General Partners, may deem advisable and shall be faithful to the partnership in all transactions relating to said business. No General Partner shall, without the written consent of all the partners, employ the capital or credit of the partnership in any other business than that of the partnership, and no partner shall, without the written consent of all the partners, during the continuation of the partnership, carry on or be concerned or interested directly or indirectly, in any other business which is in direct competition to the partnership.

6. Bankers of the Partnership. The bankers of the partnership shall be Bishop National Bank of Hawaii at Honolulu and/or such other bankers as the partners shall from time to time determine, and all money and money instruments received by and belonging to the partnership shall be deposited to the credit of the partnership with the partnership bankers, except that such a petty cash fund as may mutually be agreed upon between the General Part-

Exhibit No. 6—(Continued)

ners from time to time, may be kept on hand for use in the business.

7. Limitation on Powers of Partners. The General Partners only shall have authority to transact the business of the partnership or incur obligations or liabilities. In all matters except as otherwise provided in this Agreement, the determination by the General Partner or Partners owning the majority in interest of the capital contributed by the General Partners shall be binding upon and shall establish the policy of the partnership. The Special Partner at all times may investigate the partnership affairs and advise the General Partners as to its management. No partner shall, without the written consent of the other partners, draw, accept or sign any bill of exchange or promissory note or contract any debt on account of the partnership or employ any of the moneys or effects thereof or in any manner pledge the credit thereof except in the usual and regular course of the business subject to the provisions of this Agreement. No partner, during the continuation of this partnership, without obtaining the consent thereto of the other partners, shall assume any liability for another or others by means of endorsement or by becoming guarantor, surety or insurer, and each of the General Partners agrees at all times to keep indemnified the other partners and their personal representatives and the property of the partnership against any liability for or in connection with his present or future separate debts or engagements or actions, proceedings, claims or demands in respect thereof.

Exhibit No. 6—(Continued)

8. Partners Not to Assign Interest. No General Partner shall assign or mortgage his share of, or interest in, or any part of the share of or interest in the partnership, or the assets or profits thereof; Provided, However, that any partner may purchase all or any part of the interest of any other partner. Additional capital contributions resulting in a change in the percentage of interest of any partner, or loans or advances to the partnership on which interest is to be computed and charged for the purpose of computing net profits hereunder, as an expense of the business, may only be made with the approval of the General Partner or Partners owning the majority in interest of the capital of the partnership; Provided Further, that in the event any partner shall make additional capital contributions to the partnership, the other partners shall have the right to make similar contributions in order to keep the interest of each partner in the partnership in proportions equal to those in existence at the time of the inception of the partnership. The Special Partner may assign its share or interest in the partnership only with the consent of the General Partners evidenced by written consent attached to such assignment and filed in the office of the partnership, and the General Partners shall have full power and discretion to give or withhold such consent.

9. Books of Account and Access Thereto. Proper partnership books of account shall be kept by the

Exhibit No. 6—(Continued)

partners and entries shall be made therein of all transactions and all such matters and things as usually are entered in books of account kept by persons engaged in the same or similar businesses. Such books of account and all documents, letters, papers, instruments and records belonging to the partnership shall be kept at the office of the partnership and each partner shall, at all times, have full and free access to examine and copy the same. The books of the partnership may be audited periodically at such times as the partners shall determine, and copies of the auditor's report shall be delivered to each partner, and in such audit the capital accounts and advance accounts of the partners and of each partner shall be stated as at the end of each period.

10. Annual Accounts. A general account shall be taken annually of the assets and liabilities of the partnership, of all dealings and transactions of the same during the then preceding year, of all matters and things usually included in accounts of a like manner taken by persons engaged in like businesses, and in taking such account a just valuation shall be made of all items requiring valuation, and such annual account shall state the capital of the partnership and the interest of each partner therein at the end of the period of accounting, such general account to be sent to each partner, and unless within three (3) months any partner shall object to the same, the same shall be binding upon the partners, except for manifest errors and fraud.

Exhibit No. 6—(Continued)

11. Determination of Partnership. The partnership may be determined by a majority in interest of the General Partners at any time upon giving not less than two (2) months' previous notice in writing to the other partners of the intention of the majority in interest of the General Partners in that behalf, and at the expiration of such notice the partnership shall determine accordingly. The term "majority in interest of the General Partners" shall mean any one or more of the General Partners, the aggregate of whose capital account, as shown by the books of the partnership, shall be in excess of Fifty Per Cent (50%) of the total capital interest of all of the General Partners of the partnership. Upon the determination of the partnership from whatever cause, the General Partners agree that they will make a true, just and final account of all things relating to said business and in all things duly adjust the same. After the affairs of the partnership are adjusted, its debts paid and discharged and the expenses of liquidation shall have been paid, all of the balance then remaining shall be applied first in payment to each partner or his representative of the balance due to each partner as shown in the advance account of said partner, then in payment of his share of the capital as shown on the books of the partnership as of the close of business of the partnership, and the balance shall be divided in the same manner as hereinbefore provided for the division of profits. In the event that the balance remaining, after the payment of said

Exhibit No. 6—(Continued)

debts and expenses and the balance due to each partner as shown in the advance account of said partner, is insufficient to pay the full capital account of all the partners, then such balance shall be applied first in payment to the Special Partner of its share of the capital as shown on the books of the partnership as at the close of business of the partnership, and the balance paid to each General Partner in proportion to his capital as shown on the books of account of the partnership as at the close of business of the partnership. In the event that the balance remaining after the payment of said debts and expenses is insufficient to pay in full the balance due to each partner as shown in the advance account of each partner, then the amount shown as due to the Special Partner shall be paid first; the share of the capital of the Special Partner as shown on the books of the partnership shall be paid next, and the remaining balance, if any, shall be prorated among the General Partners according to the respective amounts shown on the books to be due on the advance account of each of said partners. The partners or their representatives shall execute such instruments for facilitating and effecting the realization and the division of the assets of the partnership and for their mutual indemnification and release and otherwise as may be requisite or proper.

12. Death of General Partner Roy Eaton. If General Partner Roy Eaton shall die before the expiration of the partnership, his representative

Exhibit No. 6—(Continued)

shall have the option (such option to be declared by notice in writing given to the surviving partners or left at the office of the partnership within six calendar months after his death) of succeeding to or carrying on the interest of the deceased partner in said business, either as a General Partner in accordance with law, or as a Special Partner under the provisions of Chapter 225, Revised Laws of Hawaii, 1935, as the same now is or as the same may from time to time be amended; and if such option shall be exercised, the said business shall be carried on during the residue of said term as from the death of said Roy Eaton, as nearly as may be according to the provisions of these presents, but so that the representative of said Roy Eaton shall succeed to his share in said business and be substituted for him as a dormant General Partner or as a Special Partner; Provided, that in case the representative of said Roy Eaton shall elect to become a dormant General Partner or a Special Partner by virtue of such option as aforesaid, all proper instruments for carrying out the provisions of this present clause shall be executed and made between his representative and the surviving partners and all proper notices, publications, petitions or court proceedings shall be made and executed or taken at the expense of the partnership.

13. Option to Purchase Share of General Partners. General Partner Roy Eaton shall have the option at any time during the term of the partnership, and his representative in the event of the death of General Partner Roy Eaton shall have the option

Exhibit No. 6—(Continued)

to purchase the interest in the partnership of any or all the other General Partners for an amount equivalent to the fair value thereof as determined by an auditor or auditors of the partnership or by the value of the interest as shown on the books of account of the partnership, whichever amount is less. In determining the fair value of such interest no value shall be attributable to good will. If said Roy Eaton or his representative shall exercise his option and the purchase is consummated, the sale shall be considered as effective on the date when the option was exercised, and the General Partner whose interest is so purchased, shall not be entitled to receive any share of the net profits from and after said date, but shall be entitled to receive interest at the current bank rate upon the amount to be paid for said General Partners' interest from said date. Said Roy Eaton or his representative shall have the right to make payment therefor by note payable in three equal annual installments with interest thereon at the current bank rate.

14. Option to Purchase Share of Deceased Partner or of General Partner Desiring to Terminate Partnership. In the event of the death of any General Partner other than Roy Eaton or of the giving of notice to terminate the partnership by any General Partner other than Roy Eaton, the said Roy Eaton shall have the option (to be exercised by notice in writing given to the Executor or Administrator, if any, or if none, then left at the office of

Exhibit No. 6—(Continued)

the partnership, or by notice in writing to the General Partner giving such notice to terminate the partnership and leaving a copy of said notice at the office of said partnership within six calendar months after the death of such General Partner or of the giving of notice to terminate the partnership, as the case may be) to purchase the interest in the partnership of such deceased General Partner or of such General Partner giving notice to terminate the partnership, for an amount equivalent to the fair value thereof as determined in accordance with the provisions of Paragraph 13 hereinabove, and all the provisions of said Paragraph 13 shall be applicable in the event that said Roy Eaton shall exercise his option to purchase the share of any other General Partner in accordance with the provisions of this paragraph.

15. Winding Up on Death of General Partner. In case the representative of said Roy Eaton shall not exercise his option to succeed to the deceased partner's share in said business as a General or a Special Partner upon the death of General Partner Roy Eaton, and in the event that upon the death of any other General Partner except said Roy Eaton, the said Roy Eaton shall not purchase the interest of said deceased General Partner, then the partnership shall be wound up at the expiration of six calendar months from the date of such death or such sooner time as the surviving partners and the representative of the deceased General Partner may

Exhibit No. 6—(Continued)

agree upon, and its affairs settled in the manner provided in Paragraph 11 hereof.

16. Bankruptcy, Etc. If any of the General Partners shall, at any time during the partnership, become incapacitated, bankrupt, insolvent or enter into any composition or arrangement with or for the benefit of his creditors, or commit any breach of any of the stipulations or agreements herein contained, the other General Partners may determine the partnership, so far as such last mentioned General Partner is concerned, by giving notice in writing left at the office of the partnership to the partner becoming incapacitated, bankrupt, insolvent or entering into such composition or arrangement or committing such breach, and may publish notice of dissolution of the partnership in regard to such last mentioned General Partner without prejudice to the remedies of the other General Partners for any antecedent breach of any of the stipulations or agreements aforesaid.

17. Arbitration. If, at any time during the continuation of the partnership or after the dissolution or determination thereof, any dispute, difference or question shall arise between the partners or their representatives touching the partnership or the accounts or transactions thereof, or the dissolution or winding up thereof, or the construction, meaning or effect of these presents, or anything herein contained, or the right or liabilities of the partners or their representatives under these presents, or otherwise in relation to the premises, then

Exhibit No. 6—(Continued)

every such dispute, difference or question shall, at the desire of any partner, be submitted to and determined by an arbitrator mutually agreed upon by all the partners; and in the event that all the partners do not agree upon the appointment of such an arbitrator within ten (10) days after any partner shall notify the other partners of his desire to have any dispute, difference or question so determined, then by three arbitrators in the manner provided by Chapter 116, Revised Laws of Hawaii, 1935, as the same now is or may from time to time be amended, in which case any partner may give to the other partners written notice of his desire to have an arbitration of the matter in dispute and name one of the arbitrators in said written notice, whereupon the other partners, within ten (10) days after the receipt of such notice, shall name a second arbitrator and in case of failure to do so the arbitrator already appointed shall name such second arbitrator, and the two arbitrators so appointed (in either manner) shall select and appoint the third arbitrator; and in the event that any two arbitrators so appointed shall fail to appoint a third arbitrator within ten (10) days after the naming of a second arbitrator, any partner may have the third arbitrator selected or appointed by the person being the Chief Justice of the Supreme Court of the Territory of Hawaii holding office at that time, and the three arbitrators so appointed shall thereupon proceed to determine the matter in question, disagreement or difference, and the decision of any two of

Exhibit No. 6—(Continued)

them (including the disposition of the costs of arbitration) shall be final, conclusive and binding upon all parties unless the same shall be vacated, modified or corrected as by said statute provided. The arbitrators shall have all the powers and duties prescribed by said statute, and judgment may be entered upon any such award by the Circuit Court of the First Judicial Circuit, as provided in said statute.

18. Amendments. If, at any time during the continuance of this partnership, the parties shall deem it necessary or expedient to make any alteration in any article, clause, matter or thing herein contained for the more advantageous or satisfactory management of the partnership business, it shall be lawful for them so to do, by any writing under their joint names, endorsed on these articles or entered in any of the partnership books, and all such alterations shall be adhered to and have the same effect, from and after the time of the adoption of the same, as if the same had originally been embodied in and formed a part of these presents.

19. Term of Partnership. The term of the partnership shall be for a period commencing with the time of execution thereof and ending September 30, 1952, and subject to the provisions of Paragraph 11 hereinabove, shall continue from year to year thereafter until terminated by any General Partner by the giving of not less than six (6) months' written notice of his intention to terminate the partner-

Exhibit No. 6—(Continued)

ship by leaving the same at the office of the partnership.

20. Definitions. The term "General Partners" as used herein shall include the heirs, executors, administrators and permitted assigns of the General Partners, and the term "Special Partner" shall include Bishop Trust Company, Limited, in its capacity as Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, and not in its individual capacity, its successors in trust and assigns.

In Witness Whereof, the parties hereto have executed these presents as of the day and year first above written.

/s/ ROY EATON,
/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.,
General Partners.

[Seal] BISHOP TRUST COMPANY, LIMITED,

Trustee Under Deed of Trust of Roy Eaton, Dated September 30, 1942, and Not Individually.

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice. Pres., Special Partner.

Exhibit No. 6—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 31st day of October, 1942, before me appeared W. A. White and E. Benner, Jr., to me personally known, who being by me duly sworn, did say that they are Vice President and Asst. Vice President, respectively, of Bishop Trust Company, Limited, Trustee under deed of trust of Roy Eaton dated September 30, 1942, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation, as such Trustee.

[Seal] /s/ THEODORA B. TOWNSEND,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, personally appeared, before me Roy Eaton, known to me to be the person described in and who executed

Exhibit No. 6—(Continued)

the foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, personally appeared before me Charles P. Johnson, known to me to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, personally appeared before me, Walter L. Prock, Jr., known to me to be the person described in and who executed the foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

EXHIBIT No. 7

Bill of Sale

This indenture, made as of the close of business on September 30, 1942, by and between Roy Eaton, of Honolulu, City and County of Honolulu, Territory of Hawaii, a citizen of the United States of America, hereinafter called the "Seller," and Nehi Beverage Company of Hawaii, a special partnership composed of Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., all of Honolulu aforesaid, all of whom are citizens of the United States of America, as General Partners, and Bishop Trust Company, Limited, a Hawaiian corporation, and a majority of whose officers and directors are citizens of the United States of America, Trustee under Deed of Trust dated September 30, 1942, made by Roy Eaton as Settlor, as Special Partner, having its principal place of business in Honolulu aforesaid, hereinafter called the "Partnership,"

Witnesseth That:

The Seller, for and in consideration of the sum of one dollar ($1.00), lawful money of the United States of America, and other good and valuable consideration to him paid, the receipt whereof is hereby acknowledged, does hereby grant, bargain, sell, assign, transfer, set over, confirm and deliver unto the Partnership and its successors and assigns forever;

All and singular, the rights, property, assets and privileges owned by the Seller and used in the business known as "Nehi Beverage Company of Ha-

Exhibit No. 7—(Continued)

waii," as shown on the balance sheet prepared by Cameron & Johnstone, dated as of the close of business on September 30, 1942, a copy of which is attached hereto, incorporated herein and made a part hereof for all purposes, including particularly but not in anywise limiting the generality of the foregoing all chattels, leaseholds, improvements, machines and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, books, accounts, inventories, together with all other personal property, goods and chattels, of every kind and description and wheresoever situate, all good will, trade names, trade connections, license, and all contracts and agreements, including any and all rights under policies of indemnity, fidelity or other bonds or insurance of any and every kind, or cash on hand or in bank or banks, bonds, mortgages, conditional sales agreements, accounts and bills receivable, promissory notes, claims, demands, equities and choses in action, and all other property and assets, tangible and intangible, of every kind or nature owned or claimed by the Seller and used by him in the business now carried on and shown on said balance sheet, save and except the consideration received by him from the partnership as the purchase price for the foregoing;

To have and to hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits and appurtenances to the same or any part thereof belonging or appertaining or held

Exhibit No. 7—(Continued)

and enjoyed therewith, unto the partnership, its successors and assigns, absolutely and forever or in fee simple as the case may be.

And the Partnership, in consideration of the foregoing, does hereby covenant and agree that it will and by these presents does assume all of the liabilities, obligations and indebtedness of the Seller, shown on said balance sheet attached hereto, and does covenant and agree to pay and discharge the same as fully and completely as though the said liabilities, obligations and indebtedness had been incurred directly by said Partnership, and to indemnify and hold harmless the said Seller from all liability, expense or obligation upon the same or arising in connection therewith;

And for the consideration aforesaid, the Seller, for himself and his heirs, executors and administrators, does hereby irrevocably appoint the Partnership, its successors and assigns, his true and lawful attorney in his name, place and stead to ask, demand, sue for and recover any and all moneys, assets or other property conveyed and transferred hereby or intended so to be and the rights and benefits therefor, and does further covenant that he, the Seller, will at any time at the request of the Partnership make, do, execute and deliver all such receipts, powers of attorney and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property, claims and demands hereinabove conveyed

Exhibit No. 7—(Continued)

and assigned or intended so to be as the partnership reasonably may require.

In witness whereof, the parties hereto have executed these presents the day and year first above written.

/s/ ROY EATON,
Seller.

NEHI BEVERAGE COMPANY OF HAWAII,
a Special Partnership,

By /s/ CHARLES P. JOHNSON,
General Partner.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Charles P. Johnson, to me personally known, who being by me duly sworn,

Exhibit No. 7—(Continued)

did say that he is a General Partner of Nehi Beverage Company of Hawaii, a special partnership; that said instrument was signed on behalf of said partnership by authority of all the partners; and that said Charles P. Johnson acknowledged said instrument to be the free act and deed of said partnership.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Nehi Beverage Company of Hawaii

Balance Sheet as at September 30, 1942

Assets

Current:			
Cash in hand and in bank..		$ 7,485.72	
Accounts receivable	$24,286.26		
Notes receivable	41.66	24,327.92	
Inventory:			
Finished goods	1,860.03		
Bottles	7,618.18		
Cases	1,717.00		
Supplies	5,039.05	16,234.26	
Special deposit		25.00	$ 48,072.90
Fixed:			
Automobiles and trucks		24,571.13	
Coolers		512.43	
Furniture and fixtures		1,842.85	
Leasehold improvements		684.23	
Machinery and equipment		47,182.00	
		74,792.64	

Exhibit No. 7—(Continued)

Less: Allowance for depreciation	20,389.50	54,403.14
Deferred:		
Office supplies	314.46	
Prepaid interest	215.69	
Prepaid taxes	883:64	
Unexpired insurance	3,070.72	4,484.51
Total Assets		$106,960.55
Liabilities		
Current:		
Accounts payable	$59,106.47	
Notes payable	12,072.34	
Accrued interest	892.43	
Accrued salaries	2,398.03	
Accrued taxes	2,491.28	$ 76,960.55
Net Worth		
Capital		30,000.00
Total Liabilities and Net Worth		$106,960.55

EXHIBIT No. 8

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of

The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

CERTIFICATE OF SPECIAL PARTNERSHIP

The undersigned, being desirous of forming a special partnership, hereby certify in accordance with the provisions of Chapter 225, Revised Laws of Hawaii 1935, as follows:

Exhibit No. 8—(Continued)

1. The name under which the partnership is to be conducted is "Nehi Beverage Company of Hawaii";

2. The general nature of the business intended to be transacted is to buy, sell, import, export, bottle, manufacture, trade and deal in beverages, extracts, syrups and goods, wares and merchandise of every kind and nature, and to carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at Kona and Hopaka Streets, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places in the Territory of Hawaii as the partners from time to time shall determine;

3. The names of the partners and the residence of each are as follows:

Roy Eaton,
General Partner, Honolulu, T. H.;

Charles P. Johnson,
General Partner, Honolulu, T. H.;

Walter L. Prock, Jr.,
General Partner, Honolulu, T. H.;

Exhibit No. 8—(Continued)

Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942,
Special Partner, Honolulu, T. H.

4. The amount of capital which the Special Partner has contributed to the special partnership assets is $15,000.00;

5. The term for which the partnership is to exist commenced on September 30, 1942, and will continue until September 30, 1952, and thereafter from year to year until terminated as provided in that certain Special Partnership Agreement dated September 30, 1942.

In witness whereof the undersigned have caused this certificate to be executed this 29th day of October, 1942.

/s/ ROY EATON,
/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.,

[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustee as Aforesaid.

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres.

Exhibit No. 8—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 31st day of October, 1942, before me appeared W. A. White and E. Benner, Jr., to me personally known, who being by me duly sworn, did say that they are Vice President and Assistant Vice President, respectively of Bishop Trust Company limited, a Hawaiian corporation Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation as such Trustee.

[Seal] /s/ THEODORA B. TOWNSEND,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the fore-

Exhibit No. 8—(Continued)

going instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Charles P. Johnson, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 29th day of October, 1942, before me personally appeared Walter L. Prock, Jr., to me known to be the person described in and who executed the

Exhibit No. 8—(Continued)

foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Received Nov. 2, 1942, Treasurer's Office, T.H.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Roy Eaton, being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated September 30, 1942, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as

Exhibit No. 8—(Continued)

aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ ROY EATON.

Subscribed and sworn to before me this 29th day of October, 1942.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Charles P. Johnson, being first duly sworn, on oath doth depose and say:

Exhibit No. 8—(Continued)

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated September 30, 1942, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ CHARLES P. JOHNSON.

Subscribed and sworn to before me this 29th day of October, 1942.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

Exhibit No. 8—(Continued)

In the Office of the Treasurer of the
Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Walter L. Prock, Jr., being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated September 30, 1942, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ WALTER L. PROCK, JR.

Exhibit No. 8—(Continued)

Subscribed and sworn to before me this 29th day of October, 1942.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

W. A. White, being first duly sworn, on oath doth depose and say:

That he is Vice President of Bishop Trust Company, Limited, a Hawaiian corporation, and as such is authorized to make this affidavit on its behalf;

That said Bishop Trust Company, Limited, is the Trustee under the Deed of Trust dated September 30, 1942, made by Roy Eaton as Settlor; that said Bishop Trust Company, Limited, a Hawaiian corporation, as Trustee under said Deed of Trust and

Exhibit No. 8—(Continued)

not in its individual capacity, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii 1935.

/s/ W. A. WHITE.

Subscribed and sworn to before me this 31st day of October, 1942.

[Seal] /s/ THEODORA B. TOWNSEND,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My Commission expires June 30, 1945.

EXHIBIT No. 9

Deed of Trust—Roy Eaton Trust No. 2

This indenture, dated this 28th day of February, 1943, by and between Roy Eaton, of Honolulu, City and County of Honolulu, Territory of Hawaii, a citizen of the United States of America, hereinafter called the "Settlor," and Bishop Trust Company, Limited (a corporation duly organized and existing under the laws of the Territory of Hawaii and a majority of whose officers and directors are citizens

Exhibit No. 9—(Continued)

of the United States of America), hereinafter called the "Trustee,"

Witnesseth That:

The Settlor, in consideration of the love and affection he bears the beneficiaries and of the acceptance by the Trustee of the trust herein created, does hereby transfer, set over and deliver to the Trustee, its successors in trust and assigns, the sum of fifteen thousand and no/100ths dollars ($15,000.00);

To have and to hold the same, together with all other property which may hereafter be or become a part of the trust estate hereby created, unto the Trustee, its successors in trust and assigns, in trust nevertheless for the uses and purposes hereinafter stated, that is to say:

(a) The Trustee shall purchase the thirty per cent (30) capital interest of the Special Partner in the partnership known as Nehi Beverage Company of Hawaii, a partnership duly organized and operating under that certain Special Partnership Agreement dated September 30, 1942, paying fifteen thousand and no/100ths dollars ($15,000.00) therefor, said amount being the fair and reasonable value of said interest duly ascertained as of February 28, 1943, and the Trustee shall become and continue to be a Special Partner therein;

(b) The Trustee shall accumulate all the net income from the said trust estate during the continuance thereof, and except as hereinafter provided, all of said net income shall be added to and

Exhibit No. 9—(Continued)

become a part of the corpus of the trust estate and be invested and reinvested as a part of said corpus during the existence of this trust;

(c) This trust shall cease and determine when the youngest of the children of the Settlor, who shall continue to survive, shall have attained the age of twenty-five (25) years, or upon the prior death of the last survivor of the said children, and the property comprising the said trust estate, together with all accumulated income thereof, shall at such time vest in and be transferred, conveyed and delivered by the Trustee, absolutely and free and clear of any trust, in equal shares to who are surviving of the children of the Settlor, and the lawful issue of any of said children who shall then be dead (said issue to take per stirpes and not per capita); and in the event that this trust shall have ceased and determined upon the death of the last survivor of the children of the Settlor, and no lawful issue of said children shall be then surviving, then the said property and income shall at such time vest in and be transferred, conveyed and delivered by the Trustee to those persons other than the Settlor, who would be the heirs-at-law of the last survivor of the children of the Settlor under the statutes of descent of the Territory of Hawaii in force and effect at the time of his or her death, the same as if he or she had died intestate at that time; provided, however, that if not terminated prior thereto, the Trustee may determine this trust at any time (but not more than one (1) year)

Exhibit No. 9—(Continued)

which to the Trustee may seem best after the Trustee shall cease to be a Special Partner in the partnership known as "Nehi Beverage Company of Hawaii," its successors and assigns;

(d) The Trustee shall receive, hold, manage and control the said trust estate, collect the income therefrom and pay all charges incident to trust estates and properly payable by said trust estate therefrom; and the Settlor authorizes the Trustee to retain either permanently or temporarily or for such period of time as it may deem expedient any property conveyed, assigned or delivered to the Trustee by the Settlor of whatever nature; and the Settlor directs that the said Trustee shall not be held liable for any loss resulting to said trust estate by reason of the Trustee's retaining any such property or for any error of judgment in this respect;

(e) The Settlor authorizes and empowers the Trustee to sell at public or private sale, convert, transfer, exchange, mortgage, hypothecate and otherwise deal in or dispose of the whole or any part of the property, real, personal or mixed, which may be from time to time a part of the trust estate, with power to accept any purchase money mortgage or mortgages for any part of the purchase or exchange price; to invest and reinvest the whole or any part of the assets of the said trust estate, and in investing and reinvesting any assets of said trust estate the Trustee may invest in common or preferred stocks of corporations, bonds, notes, debentures, participation or investment certificates and/or in any

Exhibit No. 9—(Continued)

other property, real or personal, in so far as in its judgment it shall deem such investments advisable, it being the intention of the Settlor, under the foregoing provisions, to grant to the Trustee full power to invest and reinvest money in such investments as it shall deem desirable and suitable investments for trust funds without being restricted to the classes of investments which trustees are permitted by law to make; provided, however, that the Trustee shall obtain the consent of the Settlor to make such investments during his lifetime; and provided further that in the event the Settlor shall die before the termination hereof, the Trustee shall thereafter be restricted in the making of investments of trust funds to the classes of investments which trustees are permitted by law to make, except that in any event the Trustee may, without liability for any losses resulting therefrom, make advances or loans or other or further investments in the partnership known as "Nehi Beverage Company of Hawaii," its successors and assigns; the Settlor authorizes and empowers the Trustee, upon any increase of the capital stock of any corporation in which said trust estate shall own shares, to exercise any preemptive rights to such shares to which said trust estate may be entitled and/or to subscribe for such additional shares as in the judgment of the Trustee shall be an advisable investment; and for this purpose and for other purposes of this trust, the Settlor authorizes and empowers the Trustee to borrow money either from itself or from others and upon

Exhibit No. 9—(Continued)

such terms and conditions as it may deem appropriate; the Trustee shall have the right and power to vote either directly or by proxy the stock of any corporation that may be a part of said trust estate from time to time at all meetings of stockholders as the Trustee may deem best;

(f) Stock dividends shall be treated as capital of the trust estate and all stock acquired by the Trustee under the exercise of rights to subscribe or the net proceeds realized by the Trustee from the sale of rights to subscribe shall be treated as capital of the trust estate and all other corporate distributions shall be treated as income; provided, however, that where a distribution is made through the reduction of any corporate stock held by the Trustee, or, in the exclusive discretion of the Trustee it appears to be made in or as a result of a partial or complete liquidation or dissolution of the corporation, the Trustee may in its discretion make such apportionment of any such distribution between income and capital as to it may seem just; the Trustee shall have full power and authority to decide and determine in all doubtful cases what property or moneys received by it is capital and what is income; and also in all doubtful cases to decide and determine what expenses and other charges are payable out of income and what out of capital; and also in all doubtful cases to decide and determine what proportion of payments for expenses of or charges against the trust estate are payable from income and what from capital; and all beneficiaries shall be

Exhibit No. 9—(Continued)

bound by the decision and determination of the Trustee in regard to all such allocations between capital and income; the Trustee shall have authority in and discretion to withhold such amounts of income and/or principal as it may deem necessary to protect itself from any possible liability for taxes and/or costs or expenses in connection with or arising out of possible claims therefor;

(g) The Settlor may transfer, convey and assign to the Trustee any property in addition to that hereinbefore referred to, to be held upon the trust hereby created, and thereafter such additional property shall be and form a part of the trust estate;

(h) The Trustee shall render annual statements of account to the persons who are the beneficiaries of this trust, as hereinabove provided, but the Trustee shall not be required to account in any court unless requested so to do by a beneficiary; provided, however, that the Trustee may whenever it shall deem it advisable file accounts in any court having jurisdiction thereof for approval, the costs of said proceeding to be paid out of the trust estate;

(i) If any person entitled to receive any of the income and/or corpus of the trust estate shall be a minor, the Trustee may pay the share of income and/or corpus to which said minor is entitled to either parent or to the natural or legally appointed guardian of such minor, for the account, benefit or use of such minor, and the receipt of such parent or natural or legally appointed guardian shall be a complete release, discharge and acquittance of the

Exhibit No. 9—(Continued)

Trustee to account further for any payment or payments so made, and if any beneficiary is a minor, the statements of account may be furnished to either parent or to the natural or legally appointed guardian of such minor beneficiary;

(j) The Trustee shall have the custody and safekeeping of all moneys and securities belonging to the trust estate which are received or collected by the Trustee. The Trustee may rely upon auditor's reports of the business of the partnership known as "Nehi Beverage Company of Hawaii," and shall not be required to make any independent investigation into its affairs or accounts, and the Trustee shall not be answerable or accountable for any loss or damage resulting from any error of judgment or otherwise except through its own gross negligence or wilful default, nor shall the Trustee be answerable or accountable for any loss or damage resulting from any act consented to by the Settlor or for any loss or damage resulting from any investment in or loan or advance to the partnership known as "Nehi Beverage Company of Hawaii," its successors and assigns;

(k) No beneficiary hereunder shall have the power or authority to anticipate in anywise any of the rents, issues, profits, income, moneys or payments herein provided to be devoted or paid to him or her or any part thereof, nor to alienate, encumber, convey, transfer or dispose of the same or of any interest therein or part thereof, in advance of payment; nor shall the same be involuntarily ali-

Exhibit No. 9—(Continued)

enated by him or her or be subject to attachment or execution or be levied upon or taken upon any process for any debts which any such beneficiary shall have contracted or in satisfaction of any demands or obligations which he or she shall incur. All payments or distribution of either income and/or principal as hereinabove provided shall be made by the Trustee and subject to the provisions of subparagraph (i) hereinabove shall be valid and effectual only when made to the beneficiary to whom the same shall appertain and belong, and upon his or her individual receipt; provided, however, that when and while the person so entitled to receive such payment shall be without the bounds of the Territory of Hawaii, such payment may be made to any formally appointed agent of such person, but only upon the personal receipt above provided for;

(1) It is hereby declared that this agreement shall be and is hereby made irrevocable by the Settlor and the Settlor reserves the right to amend this instrument only by adding other property to be and become a part of the estate held under the terms hereof, and the right to alter, amend, cancel or revoke any provisions of this instrument, save and except paragraphs (a), (b) and (c) hereof; provided, however, that in no event shall any of the property or the income thereof belonging to the trust estate be paid to or inure to the benefit of the Settlor, and provided further that any amendments made by the Settlor shall be made by instrument in writing and acknowledged and filed with

Exhibit No. 9—(Continued)

the Trustee, and that the alteration, amendment, cancellation or revocation of any provision of this instrument shall be made only with the written consent and approval of the Trustee;

The said Bishop Trust Company, Limited, hereby accepts the within trust and covenants and agrees with the Settlor that it will faithfully discharge and carry out the same.

In witness whereof, the parties hereto have executed these presents the day and year first above written.

/s/ ROY EATON,
Settlor.

[Seal] BISHOP TRUST COMPANY, LIMITED,

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres., Trustee.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 22nd day of April, 1943, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Exhibit No. 9—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 24th day of April, 1943, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Asst. Vice Pres., respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

EXHIBIT No. 10

Assignment

Assignment of Partnership Interest in Nehi Beverage Company of Hawaii—Roy Eaton Trust No. 2

This indenture, made this 28th day of February, 1943, by and between Bishop Trust Company, Limited, a Hawaiian corporation, a majority of whose officers and directors are citizens of the United

Exhibit No. 10—(Continued)

States of America, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, hereinafter called the "assignor," and Bishop Trust Company, Limited, a Hawaiian corporation, a majority of whose officers and directors are citizens of the United States of America as aforesaid, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943, hereinafter called the "Assignee,"

Witnesseth That:

The Assignor, for and in consideration of the sum of fifteen thousand and no/100ths dollars ($15,000.00), lawful money of the United States of America, and other good and valuable consideration to it paid, the receipt of which is hereby acknowledged, does hereby assign, transfer, set over, and deliver unto the Assignee, its successors and assigns in trust, all of its right, title and interest in and to its thirty (30) per cent capital interest of the special partnership known as "Nehi Beverage Company of Hawaii," a partnership duly organized and operating under that certain Special Partnership Agreement dated September 30, 1942, provided, however, that nothing herein contained shall constitute an assignment of any of its right to the advance account covering the share of the Assignor in the undivided profits of said special partnership to February 28, 1943.

To have and to hold the same unto the Assignee, its successors and assigns in trust, absolutely,

And Roy Eaton, Charles P. Johnson, and Walter

Exhibit No. 10—(Continued)

L. Prock, Jr., all of whom are citizens of the United States of America, of Honolulu, City and County of Honolulu, Territory of Hawaii, being all the General Partners in said Special Partnership known as "Nehi Beverage Company of Hawaii," hereby consent to the assignment of said partnership interest as herein provided.

In witness whereof, the parties hereto have executed these presents as of the day and year first above written.

[Seal] BISHOP TRUST COMPANY, LIMITED,

Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, and Not Individually.

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres.

/s/ ROY EATON,

/s/ CHARLES P. JOHNSON,

/s/ WALTER L. PROCK, JR.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 22nd day of April, 1943, personally appeared before me Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., known to me to be the persons described in and who executed the fore-

Exhibit No. 10—(Continued)

going instrument and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 24th day of April, 1943, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and the Assistant Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation as Trustee aforesaid by authority of its Board of Directors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

EXHIBIT No. 11

Amendment of Special Partnership Agreement
(Roy Eaton Trust No. 2)

This indenture, made this 28th day of February, 1943, by and between Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., all of whom are citizens of the United States of America, of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter referred to as "General Partners," and Bishop Trust Company, Limited, a Hawaiian corporation, and a majority of whose officers and directors are citizens of the United States of America, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, hereinafter referred to as the "Special Partner,"

Witnesseth That:

Whereas the General Partners and Bishop Trust Company, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, as Special Partner, have formed with each other a Special Partnership by Special Partnership Agreement dated September 30, 1942; and

Whereas the interest of said Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, has been purchased by Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943, and the General Partners have consented to said assignment; and

Whereas the parties hereto deem it necessary to

(Exhibit No. 11—(Continued)

alter certain provisions in accordance with the provisions of Paragraph 18, Pages 14 and 15, in said Special Partnership Agreement contained,

Now, Therefore, This Indenture Witnesseth:

1. That said Special Partnership Agreement is hereby altered by substituting "Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943," as Special Partner in the place and stead of "Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942."

2. That Paragraph 4 of said Special Partnership Agreement is hereby altered to read as follows:

"Compensation of General Partners and Division of Profits. From time to time, and as the General Partners may agree, the General Partners actively engaged in the business of the partnership shall receive, as compensation for services rendered to the partnership, a salary chargeable for purposes of computing net profits hereunder, as an expense of the business, in such amount as the General Partners may from time to time agree upon, constituting the reasonable value of the services rendered to the partnership. All of the remaining net profits of the partnership shall be divided for each annual period in proportion to the above stated interest of each of the partners in the original capital of the partnership, and all losses of the partnership for each annual period shall be divided among

(Exhibit No. 11—(Continued)

the partners in the same manner as herein provided for the division of profits, provided, however, that General Partners Charles P. Johnson and/or Walter L. Prock, Jr., shall only be entitled to such amount of the net profits of the business during any period of time in which the business of the partnership is not the principal activity of said partner, as is not in excess of 12% per annum of the amount of said General Partner's capital interest, and the remaining net profits of the partnership shall be divided in proportion to the above stated interest of each of the other partners in the original capital of the partnership. Profits and losses that may arise out of or occur in the prosecution of the said partnership operations, shall be credited or charged at the close of each year on the books of the partnership to the account of each partner in proportion to the account of each partner, but none of the said profits or capital shall be withdrawn by any partner (save and except that sufficient thereof may be withdrawn by the Special Partner to pay all taxes, commissions, fees, and expenses payable on the profits of said Special Partner or payable on account of the investment by the Special Partner of trust assets in said partnership, and by the General Partners to pay all taxes payable on the profits of said General Partners) until the capital of the partnership shall exceed $100,000.00, and then only to the extent of each partner's share of such excess."

In witness whereof, the parties hereto have

(Exhibit No. 11—(Continued)

executed these presents as of the day and year first above written.

/s/ ROY EATON,
/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.,
General Partners.

[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustee Under Deed of Trust of Roy Eaton, Dated February 28, 1943, and Not Individually.

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres.,
Special Partner.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 22nd day of April, 1943, personally appeared before me Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., known to me to be the persons described in and who executed the foregoing instrument and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

(Exhibit No. 11—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 24th day of April, 1943, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and the Assistant Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation as Trustee aforesaid by authority of its Board of Directors and said W. A. White and E. Benner, Jr, acknowledged said instrument to be the free act and deed of said corporation as such Trustee.

/s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

EXHIBIT No. 12

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

CERTIFICATE OF CHANGE OF SPECIAL PARTNERSHIP

The undersigned, a Special Partnership, hereby certify in accordance with the provisions of Chapter 225, Revised Laws of Hawaii, 1935, as follows:

1. The name under which the partnership is to be conducted is "Nehi Beverage Company of Hawaii";

2. The general nature of the business intended to be transacted is to buy, sell, import, export, bottle, manufacture, trade and deal in beverages, extracts, syrups and goods, wares and merchandise of every kind and nature, and to carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at Kona and Hopaka Streets, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such

Exhibit No. 12—(Continued)

other place or places in the Territory of Hawaii as the partners from time to time shall determine;

3. The names of the partners and the residence of each are as follows:

General Partners

Roy Eaton,
2112 Mott-Smith Dr., Honolulu, T. H.

Charles P. Johnson,
Mariposa Road, Honolulu, T. H.

Walter L. Prock, Jr.,
2373 Hoomaha Way, Honolulu, T. H.

Special Partner

Bishop Trust Company, Limited in its capacity as Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943, and not in its individual capacity.
Bishop Trust Building, corner of Bishop and King Streets, Honolulu, T. H.

Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, dated September 30, 1942, has withdrawn from the Special Partnership;

4. The amount of capital which the Special Partner has contributed to the partnership assets is $15,000.00;

5. The change in the Special Partnership became effective on February 28, 1943. The Special Partnership will continue until September 30, 1952,

Exhibit No. 12—(Continued)

and thereafter from year to year until terminated as provided in that certain Special Partnership Agreement dated September 30, 1942.

In witness whereof, the undersigned have caused this certificate to be executed this 22nd day of April, 1943.

/s/ ROY EATON,
/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.

[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustee as Aforesaid.

By /s/ W. A. WHITE,
Its Vice President.

By /s/ E. BENNER, JR.,
Its Asst. Vice Pres.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 22nd day of April, 1943, before me personally appeared Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., to me known to be the persons described in and who executed the foregoing instrument, and acknowledged that they executed the same as their free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Exhibit No. 12—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 24th day of April, 1943, before me appeared W. A. White and E. Benner, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Assist. Vice-Pres., respectively of Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943, the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said W. A. White and E. Benner, Jr., acknowledged said instrument to be the free act and deed of said corporation as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Received April 26, 1943, Treasurer's Office, T. H.

Exhibit No. 12—(Continued)

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of:

The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Roy Eaton, being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated February 28, 1943, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ ROY EATON.

Exhibit No. 12—(Continued)

Subscribed and sworn to before me this 22nd day of April, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of:

The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Charles P. Johnson, being first duly sworn, on oath doth depose and say:

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated February 28, 1943, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a

Exhibit No. 12—(Continued)

capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ CHARLES P. JOHNSON.

Subscribed and sworn to before me this 22nd day of April, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of:

The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

Walter L. Prock, Jr., being first duly sworn, on oath doth depose and say:

Exhibit No. 12—(Continued)

That he is a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; that Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust dated February 28, 1943, made by Roy Eaton as Settlor, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the requirements of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ WALTER L. PROCK, JR.

Subscribed and sworn to before me this 22nd day of April, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

Exhibit No. 12—(Continued)

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of:

The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII.

AFFIDAVIT OF SPECIAL PARTNERSHIP REQUIRED BY SECTION 6875, REVISED LAWS OF HAWAII, 1935

Territory of Hawaii,
City and County of Honolulu—ss.

W. A. White, being first duly sworn, on oath doth depose and say:

That he is Vice President of Bishop Trust Company, Limited, a Hawaiian corporation, and as such is authorized to make this Affidavit on its behalf;

That said Bishop Trust Company, Limited, is the Trustee under the Deed of Trust dated February 28, 1943, fade by Roy Eaton as Settlor; that said Bishop Trust Company, Limited, a Hawaiian corporation, as Trustee under said Deed of Trust and not in its individual capacity, is a Special Partner in the partnership of Nehi Beverage Company of Hawaii; that as Special Partner said Bishop Trust Company, Limited, Trustee as aforesaid, actually has paid into the partnership as a capital contribution the sum of $15,000.00 in lawful money;

And further affiant sayeth not except that this Affidavit is made in accordance with the require-

Exhibit No. 12—(Continued)

ments of the provisions of Section 6875, Revised Laws of Hawaii, 1935.

/s/ W. A. WHITE.

Subscribed and sworn to before me this 24th day of April, 1943.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945.

EXHIBIT No. 13

Bill of Sale

This Indenture made as at the close of business on June 30, 1946, by and between Charles P. Johnson of Honolulu, City and County of Honolulu, Territory of Hawaii, and Walter L. Prock, Jr., of Honolulu aforesaid, hereinafter called the "Sellers," and Roy Eaton of Honolulu aforesaid, hereinafter called the "Purchaser,"

Witnesseth That:

Whereas the Sellers and the Purchaser are general partners in that certain special partnership registered to do and doing business in the Territory of Hawaii under the name of Nehi Beverage Company of Hawaii, which said partnership consists of the parties hereto as general partners, and Bishop

Exhibit No. 13—(Continued)

Trust Company, Limited, as Trustee under Deed of Trust dated February 28, 1943, as special partner; and

Whereas, in accordance with the articles of copartnership the Sellers desire to withdraw as partners from said partnership, and have agreed to sell to the Purchaser, and the Purchaser has agreed to buy from the Sellers their respective interests in said partnership,

Now, Therefore, the Sellers for and in consideration of the sum of Ten Dollars ($10.00) and other good and valuable consideration, the receipt whereof is hereby acknowledged, do hereby assign, transfer, set over, bargain, sell, grant and deliver unto the Purchaser, his heirs and assigns absolutely;

All and singular the rights, property, assets and privileges owned by the Sellers and constituting their respective interests in the special partnership known as Nehi Beverage Company of Hawaii, a partnership duly organized and operating under that certain special partnership agreement dated September 30, 1942, said interests being as shown on the balance sheet prepared by Cameron & Johnstone, Certified Public Accountants, auditors of the partnership, dated as of the close of business on June 30, 1946, copy of which is on file in the office of the partnership and which is incorporated herein and by reference made part hereof for all purposes, including particularly, but not in any wise limiting the generality of the foregoing, all their right and

Exhibit No. 13—(Continued)

interest in all chattels, leaseholds, improvements, machines and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, books, accounts, inventories, together with all other personal property, goods and chattels, of every kind and description, and wheresoever situate; all good will, trade names, trade connections, licenses, and all contracts and agreements, including any and all rights under policies of indemnity, fidelity or other bonds or insurance of any and every kind, or cash on hand or in bank or banks, bonds, mortgages, conditional sales agreements, accounts and bills receivable, promissory notes, claims, demands, equities and choses in action, and all other property and assets, tangible and intangible, of every kind or nature owned or claimed by the Sellers or either of them, and used in the business conducted by said partnership.

To Have and to Hold the same, together with all improvements, rights, easements, privileges, rents, issues, profits and appurtenances to the same or any part thereof belonging or appertaining to or held and enjoyed therewith, unto the Purchaser, his heirs, executors, administrators and assigns, absolutely and forever or in fee simple as the case may be;

And, for the consideration aforesaid, the Sellers do severally for themselves and their respective heirs, executors and administrators, hereby irrevocably appoint the Purchaser, his heirs and assigns, the true and lawful attorney for them and

Exhibit No. 13—(Continued)

each of them, in their respective names, places and steads to ask, demand, sue for and recover any and all assets and other property conveyed and transferred hereby or intended so to be, and the rights and benefits therefor, with full power to make, execute and deliver for and on their behalf, and on behalf of each of them, all such certificates, receipts, bills of sale, and such other instruments as may be necessary or proper for the better and more effectual vesting and confirming of all right and interest, property, claims and demands hereinabove conveyed and assigned or intended so to be as the Purchaser may reasonably require or as the said partnership may reasonably require, for the purpose of effectuating the withdrawal of said Sellers from said partnership;

And the Purchaser does hereby covenant and agree that he will indemnify and save harmless the Sellers and each of them from any liability of any kind or nature arising out of any obligation, indebtedness or claim however arising and payable by said partnership whether now or hereafter shown on the books of account of said partnership;

And the parties hereto do mutually agree that the account prepared by Cameron & Johnstone, Certified Public Accountants, for the partnership for the period ending June 30, 1946, shall be and it is hereby accepted and approved as an Account Stated, and do hereby mutually release each other from all further liability, claim or obligation of any kind except as herein provided and except as pro-

Exhibit No. 13—(Continued)

vided in the promisory notes delivered by the Purchaser to the Sellers concurrently herewith, arising out of or in connection with the formation, operation or modification of said partnership or in any manner connected therewith.

In Witness Whereof, the parties hereto have executed these presents the day and year first above written.

/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.,
Sellers.

/s/ ROY EATON,
Purchaser.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of September, 1946, before me personally appeared Charles P. Johnson to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARY B. GARDNER,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1948.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of September, 1946, before me personally appeared Walter L. Prock, Jr., to me known to be the person described in and who exe-

Exhibit No. 13—(Continued)

cuted the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARY B. GARDNER,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1948.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 11th day of September, 1946, before me personally appeared Roy Eaton to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

EXHIBIT No. 14

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of:
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII.

CERTIFICATE OF CHANGE OF SPECIAL PARTNERSHIP

The undersigned, a Special Partnership, hereby certify in accordance with the provisions of Chap-

Exhibit No. 14—(Continued)

ter 225, Revised Laws of Hawaii, 1935, as amended, as follows:

1. The name under which the partnership is now and will be conducted is "Nehi Beverage Company of Hawaii";

2. The general nature of the business transacted is to buy, sell, import, export, bottle, manufacture, trade and deal in beverages, extracts, syrups and goods, wares and merchandise of every kind and nature and to carry on the business of general wholesale and retail merchants, importers, exporters, commission merchants, brokers, factors, agents or manufacturers and such other business as may be necessary, suitable or proper to the accomplishment of the purposes or connected with or related thereto as the partners from time to time mutually may agree; and the place or places where the business is to be transacted is at Kona and Hopaka Streets, Honolulu, City and County of Honolulu, Territory of Hawaii, and/or at such other place or places in the Territory of Hawaii as the partners from time to time shall determine;

3. The names of the parties and the addresses of each are as follows:

General Partner

ROY EATON,
140 Dowsett Avenue,
Honolulu, T. H.

Exhibit No. 14—(Continued)

Special Partner

BISHOP TRUST COMPANY, LIMITED, Trustee,
King & Bishop Streets
Honolulu, T. H.

That a change has occurred in said partnership in that Charles P. Johnson and Walter L. Prock, Jr., general partners, have withdrawn as partners from the special partnership and their interests have been assigned to Roy Eaton who will continue as a general partner;

4. The amount of capital which the special partner has contributed to the partnership assets is Fifteen Thousand Dollars ($15,000.00), as appears by affidavit heretofore filed in the Office of the Treasurer, Territory of Hawaii;

5. The change in the special partnership will become effective on the filing of this certificate, but said change and the assignments referred to in Paragraph 3 hereof have been dated as of June 30, 1946; the special partnership will continue until September 30, 1952, and thereafter from year to year until terminated, as provided in that certain special partnership agreement dated September 30, 1942.

In Witness Whereof the undersigned have caused

Exhibit No. 14—(Continued)

this certificate to be executed this 11th day of September, 1946.

/s/ ROY EATON,
/s/ CHARLES P. JOHNSON,
/s/ WALTER L. PROCK, JR.

[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustee as Aforesaid.

By /s/ E. BENNER, JR.,
Its Vice-Pres.

By /s/ T. G. SINGLEHURST,
Its Treasurer.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 11th day of September, 1946, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of September, 1946, before me personally appeared Charles P. Johnson, to me

Exhibit No. 14—(Continued)

known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARY B. GARDNER,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1948.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of September, 1946, before me personally appeared Walter L. Prock, Jr., to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ MARY B. GARDNER,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1948.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 11th day of September, 1946, before me appeared E. Benner, Jr., and T. G. Singlehurst to me personally known, who, being by me duly sworn, did say that they are the Vice President and Treasurer, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton, dated February 28, 1943,

Exhibit No. 14—(Continued)

the corporation described in the foregoing instrument, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors and said E. Benner, Jr., and T. G. Singlehurst acknowledged said instrument to be the free act and deed of said corporation as such Trustee.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

EXHIBIT No. 15

Honolulu, T. H.
October 11, 1946.

Mr. Roy Eaton and
Bishop Trust Company, Limited
Trustee under Deed of Trust of
Roy Eaton dated February 28, 1943,
Copartners Doing Business as
Nehi Beverage Company of Hawaii,
Kona and Hopaka Streets
Honolulu, T. H.

Gentlemen:

This will confirm our agreement made for and on behalf of a corporation to be organized as herein provided (herein called the "purchasing corporation") to purchase from you all of the assets, prop-

Exhibit No. 15—(Continued)

erty and business known as Nehi Beverage Company of Hawaii under the following terms and conditions:

(1) The property sold shall include all machinery, equipment, leaseholds, bottles and cases, supplies, furniture, motor vehicles, accounts receivable, and all other property of every kind and nature used in your business, as shown on the books of said partnership (including the franchises, trade names and good will, which are referred to hereinbelow).

(2) The purchase price for all assets (other than the franchises, trade names and good will) shall be equal to the adjusted net book value of the assets as shown on the audit statement to be prepared as of September 30, 1946, by Messrs. Cameron & Johnstone, certified public accountants. It is our agreement that sufficient cash will be withdrawn from the partnership assets prior to the effective date of the sale so that the purchase price to the purchasing corporation for the physical assets (after withdrawal of cash computed as herein provided) shall be $100,000.00; and the purchasing corporation shall assume and promptly pay and discharge all obligations and indebtedness of the partnership as shown in the books of account of said partnership.

(3) It is understood that the purchasing corporation and the sellers will adjust the net book value of the assets either upward or downward in the event the auditors shall determine that the net book

Exhibit No. 15—(Continued)

value of the assets sold require an adjustment by reason of items or facts not now recorded in the books of the partnership; provided, however, that all tax claims, tax refunds, tax liabilities for business transacted prior to October 1, 1946, shall be for the sole account of the sellers, and the assets shall not be deemed to include a refund from Nehi Beverage Corporation, of advertising expense incurred prior to September 30, 1946, nor include other accruals arising out of the operation of the business prior to September 30, 1946, not recorded on the books of the partnership. The purchasing corporation will accept the physical assets in the condition they are in upon the date of delivery, without representations or warranties (other than warranty of title), a full examination having been made on behalf of the purchasing corporation.

(4) It is our understanding that the three franchises together with the good will and trade names "Nehi Beverages," "Royal Crown Cola" and "Par-T-Pak" have been issued by Nehi Corporation of Columbus, Georgia, and are held in the name of Roy Eaton, said franchises being exclusive franchises covering the Territory of Hawaii.

We have agreed to purchase said franchises (and the good will and trade names connected therewith) for an additional amount of $135,000.00 payable by the purchasing corporation as hereinbelow provided.

(5) The sale shall be effective as of October 1, 1946, all accruals and all expenses and obligations

Exhibit No. 15—(Continued)

from and after said date to be for the account of the purchasing corporation.

(6) Terms of Payment: The purchasing corporation agrees to pay for the physical assets purchased, as follows:

Upon execution of a bill of sale to the purchasing corporation covering all assets, other than franchises, trade names and good will, the purchasing corporation shall pay the sum of $65,000.00 in cash and to deliver promissory notes duly executed by the purchasing corporation payable severally to Roy Eaton and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, in installments in the aggregate principal amount of $35,000.00, payable as shown on the schedule attached hereto and made part hereof for every purpose.

The purchasing corporation agrees to pay for the franchises (including good will and trade names) as follows:

Upon written confirmation that the Nehi Corporation of Columbus, Georgia, will issue the three franchises above referred to into the name of H. C. Lundburg, the purchasing corporation will pay $5,000.00 in cash and will deliver promissory notes duly executed by the purchasing corporation payable severally to Roy Eaton and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, in installments in the aggregate principal amount of $130,000.00

Exhibit No. 15—(Continued)

payable as shown on schedule attached hereto and made part hereof for every purpose.

(7) We undertake and agree upon approval hereof to cause to be formed a Hawaiian corporation to be known as Nehi Beverage Company of Hawaii, Ltd., or having a substantially similar name, said corporation to have a capital of not less than $115,000.00 fully paid in; that the purchase herein agreed to shall be made by said corporation; that the promissory notes above referred to shall be executed by said Nehi Beverage Company of Hawaii, Ltd., but without endorsement or guarantee by the undersigned; that upon the execution of the promissory notes all of the issued and outstanding stock of said corporation shall be pledged to secure the repayment of said promissory notes, but with no power in the pledgees to vote said stock except upon default; that the purchasing corporation will covenant and agree at all times to abide by the terms and conditions of the franchises and to keep said franchises in full force and effect; that the purchasing corporation will not engage in any business without the written consent of the Nehi Corporation, except the businesses necessary to maintain and operate the said franchises; that the purchasing corporation shall have the option at any time of paying the promissory notes in full; that in the event that the purchasing corporation shall default in any of the terms or conditions hereof, or in making the installment payments when due, then the

Exhibit No. 15—(Continued)

entire deferred balance on the promissory notes shall be due and payable, together with costs of collection and reasonable attorney's fees.

(8) The sellers agree to make, execute and deliver all such assignments, bills of sale and instruments of conveyance as may be necessary to carry the foregoing agreement into effect and that the transfer and delivery shall be effected within thirty (30) days from the date hereof, or within ten (10) days after completion of the audit, whichever date shall be later, it being understood, however, that the transaction shall be completed as soon as reasonably practicable.

(9) We have deposited this day $10,000.00 with your attorneys, Smith, Wild, Beebe & Cades, to be held as security for our undertakings hereunder, said deposit to be returned to the undersigned in the event that the Sellers shall not perform or be able to perform their agreement as hereinbefore set forth, or if Nehi Corporation (Georgia) shall fail or refuse to issue said three (3) franchises to H. C. Lundburg, or in the event that the purchasing corporation shall make the initial payments and execute promissory notes as required hereinabove. Time is of the essence of this contract and in the event that the undersigned or the purchasing corporation shall fail or neglect to carry out their undertakings in accordance with the terms hereof, Smith, Wild, Beebe & Cades are authorized to pay said $10,000.00 to the Sellers as liquidated dam-

Exhibit No. 15—(Continued)

ages and not as a penalty and the Sellers shall have no further obligation hereunder of any kind, or in the alternative, to file a bill of interpleader in the Circuit Court of the First Judicial Circuit, Territory of Hawaii, and deposit said sum of $10,000.00, less any expenses incurred, with the Clerk of said Court, and upon so doing, Smith, Wild, Beebe & Cades shall be released of and from all further obligations with respect thereto, and all questions of damages shall be determined by said court.

(10) It is agreed that the promissory notes hereinbefore referred to shall not bear interest.

(11) It is further agreed:

A. That the cost of auditing hereinbefore referred to and all legal expenses incurred by the Sellers with respect to the foregoing agreement and the preparation and execution of the bill of sale, promissory notes and collateral pledge agreements hereinbefore referred to shall be paid by the sellers, and that legal expenses incurred by the Purchasers with respect to the foregoing agreement or in the preparation and execution of documents which may be necessary to carry out their part of said agreement shall be paid by the Purchasers;

B. That if prior to the date when legal title or possession of the subject matter of the foregoing contract shall have been transferred, all or a material part thereof shall be destroyed without fault of the Purchasers, said agreement shall forthwith terminate and the Purchasers shall be entitled to recover the said sum of $10,000.00 which has been

Exhibit No. 15—(Continued)

so deposited with the firm of Smith, Wild, Beebe & Cades.

(12) Roy Eaton agrees that without additional compensation, he will for a period of thirty (30) days from and after the date of execution of the bill of sale above referred to devote all of his time and attention during usual business hours in assisting the Purchasers with respect to the proper management and conduct of said business.

Very truly yours,

/s/ H. C. LUNDBURG,

/s/ K. J. LUKE,

/s/ Y. O. LEONG,

Purchasers.

The foregoing agreement is hereby accepted and approved.

/s/ ROY EATON.

BISHOP TRUST COMPANY, LIMITED,
Trustee as Aforesaid,

By /s/ W. A. WHITE,
Its Vice Pres.

By /s/ G. W. FISHER,
Its Vice Pres., Co-Partners Doing Business as Nehi Beverage Company of Hawaii.

Exhibit No. 15—(Continued)

Schedule of Deferred Payments
for Physical Assets

Date of Deferred Payment	To— Roy Eaton	To— Bishop Trust Company, Limited, Trustee
Jan. 2, 1947	$21.000.00	$ 9,000.00
Oct. 1, 1947	3,500.00	1,500.00
	$24,500.00	$10,500.00

Schedule of Deferred Payments for Franchises
(Including Trade Names and Good Will)

Date of Deferred Payment	To— Roy Eaton	To— Bishop Trust Company, Limited, Trustee
Oct. 1, 1947	$ 4,900.00	$ 2,100.00
Apr. 1, 1948	4,200.00	1,800.00
Oct. 1, 1948	4,200.00	1,800.00
Apr. 1, 1949	4,200.00	1,800.00
Oct. 1, 1949	4,200.00	1,800.00
Apr. 1, 1950	4,200.00	1,800.00
Oct. 1, 1950	4,200.00	1,800.00
Apr. 1, 1951	4,200.00	1,800.00
Oct. 1, 1951	4,200.00	1,800.00
Apr. 1, 1952	4,200.00	1,800.00
Oct. 1, 1952	4,200.00	1,800.00
Apr. 1, 1953	4,200.00	1,800.00
Oct. 1, 1953	4,200.00	1,800.00
Apr. 1, 1954	4,200.00	1,800.00
Oct. 1, 1954	4,200.00	1,800.00
Apr. 1, 1955	4,200.00	1,800.00
Oct. 1, 1955	4,200.00	1,800.00
Apr. 1, 1956	4,200.00	1,800.00
Oct. 1, 1956	4,200.00	1,800.00
Apr. 1, 1957	4,200.00	1,800.00
Oct. 1, 1957	4,200.00	1,800.00
Apr. 1, 1958	2,100.00	900.00
	$91,000.00	$39,000.00

EXHIBIT No. 16

Bill of Sale

This Indenture made as of the opening of business on the 1st day of October, 1946, by and between Nehi Beverage Company of Hawaii, a registered special partnership (composed of Roy Eaton, general partner, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust made by Roy Eaton, Settlor, dated February 28, 1943, special partner), hereinafter called the "Seller," and Nehi Beverage Company of Hawaii, Ltd., a corporation organized under the laws of the Territory of Hawaii, hereinafter called the "Purchaser,"

Witnesseth That:

Whereas the Seller is the owner of that certain business conducted by and under the name of "Nehi Beverage Company of Hawaii"; and

Whereas the general partner is the owner and holder of three franchises together with the trade names and good will connected with "Nehi Beverage," "Royal Crown Cola" and "Par-T-Pak" which said franchises have been issued by Nehi Corporation of Columbus, Georgia, and which said franchises are exclusive franchises covering the Territory of Hawaii, and are all held by said general partner for the account and benefit of said special partnership; and

Whereas concurrently herewith the general partner, for valuable consideration, has caused the said franchises (together with the attendant good will

Exhibit No. 16—(Continued)

and trade names) to be issued into the name of H. C. Lundburg and the said Seller has agreed to make, execute and deliver all such assignments, bills of sale and instruments of conveyance as may be necessary to transfer and deliver unto the Purchaser all of the assets and properties hereinafter described;

Now, Therefore, in consideration of Ten Dollars ($10.00) and other good and valuable consideration, receipt whereof is hereby acknowledged, the Seller does hereby assign, transfer, set over, deliver and confirm unto the Purchaser, its successors and assigns:

All and singular the rights, property, assets and privileges owned by the Seller and used in the business carried on by it referred to and identified as assets on "Exhibit A Nehi Beverage Company of Hawaii Balance Sheet, September 30, 1946" prepared by Messrs. Cameron & Johnstone, Certified Public Accountants, which is hereto attached and made part hereof for every purpose, including particularly, but not in any wise limiting the generality of the foregoing, all chattels, leaseholds, improvements, machines, and equipment, all furniture, office equipment, office machinery, appliances and devices, all files, records, accounts and inventories, toegther with all other personal property, goods and chattels of every kind and description in said Exhibit A referred to, wheresoever situate, all contracts and agreements, including any and all rights under policies of indemnity, fidelity or any other

Exhibit No. 16—(Continued)

bonds and insurance of any and every kind, all cash on hand or in bank or banks (excluding, however, the sum of $25,513.69 not transferred hereby), conditional sale agreements, bills receivable, promissory notes, claims, demands, equities and choses in action.

To Have and to Hold the same, together with all improvements, rights, easements, privileges, rents, issues and profits, and appurtenances to the same or any part thereof belonging or appertaining or held and enjoyed therewith, unto the Purchaser, its successors and assigns, absolutely and forever.

And the Purchaser does hereby covenant and agree that it will and by these presents does assume all of the liabilities, obligations and indebtedness of the Seller arising out of or in connection with the operation of said business prior to September 30, 1946, and identified as liabilities on said Exhibit A, together with all liabilities, obligations, and indebtedness arising out of or in connection with the operation of the business after said date, and does covenant and agree to pay and discharge the same as fully and completely as though said liabilities, obligations and indebtedness had been incurred directly by said Purchaser, and to indemnify and hold harmless the said Seller from all liability, expense and obligation upon the same arising in connection therewith.

And for the consideration aforesaid, the Seller does hereby covenant with said Purchaser that the Seller is the lawful owner of all of the above-described property and has good right to sell and

Exhibit No. 16—(Continued)

assign the same as aforesaid and that the Seller will and its successors and assigns shall warrant and defend unto the Purchaser, its successors and assigns, forever, the above-described property against the claims and demands of all persons claiming by, through or under said Seller, provided, however, that said Bishop Trust Company, Limited, as Trustee aforesaid, shall not be liable under this covenant beyond its present interest in and the proceeds from the sale of the assets and property of said special partnership.

And for the consideration aforesaid, the Seller, for itself and its successors and assigns, does hereby irrevocably appoint the Purchaser, its successors and assigns, its true and lawful attorney, in its name, place and stead to ask, demand, sue for and recover any and all moneys, assets or other property conveyed and transferred hereby or intended so to be, and the rights and benefits therefor, and does further covenant that it, the Seller, will at any time at the request of the Purchaser make, do, execute and deliver all such receipts, powers of attorney, and further instrument or instruments for the better and more effectual vesting and confirming of all right and interest, property claims and demands hereinabove conveyed and assigned or intended so to be as the Purchaser reasonably may require.

And the Purchaser and the Seller mutually agree that all tax claims, tax refunds, tax liabilities for business transacted prior to October 1, 1946, shall be the sole property and for the sole account of the

Exhibit No. 16—(Continued)

Seller and that the transfer hereby made shall not be deemed to include refund from Nehi Beverage Corporation of advertising expense incurred prior to September 30, 1946, nor include other accruals arising out of the operation of the business prior to September 30, 1946, and not referred to or included on said Exhibit A.

In Witness Whereof the parties hereto have executed these presents as of the day and year first above written.

/s/ ROY EATON,
General Partner.

[Seal] BISHOP TRUST COMPANY, LIMITED,
Trustee as Aforesaid.

By /s/ E. BENNER, JR.,
Its Vice Pres.

By /s/ G. H. VICARS, JR.,
Its Asst. Vice Pres.,
Special Partner; Seller.

NEHI BEVERAGE COMPANY OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer,
Purchaser.

Exhibit No. 16—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the foregoing instrument and duly acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me appeared E. Benner, Jr., and G. H. Vicars, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Assistant Vice President, respectively, of Bishop Trust Company, Limited, Trustee under Deed of Trust made by Roy Eaton, Settlor, dated February 28, 1943, a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr., and G. H. Vicars, Jr., acknowl-

Exhibit No. 16—(Continued)

edged said instrument to be the free act and deed of said corporation as Trustee aforesaid.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me appeared H. C. Lundburg and Kan Jung Luke, to me personally known, who, being by me duly sworn, did say that they are the President and Secretary-Treasurer, respectively, of Nehi Beverage Company of Hawaii, Ltd., a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said H. C. Lundburg and Kan Jung Luke acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

EXHIBIT No. 17

Assignment of Lease

This Indenture, made as of the opening of business on the 1st day of October, 1946, by and between Nehi Beverage Company of Hawaii, a registered special partnership (composed of Roy Eaton, general partner, and Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust made by Roy Eaton, Settlor, dated February 28, 1943, special partner) hereinafter called the "Assignor," and Nehi Beverage Company of Hawaii, Ltd., a corporation organized under the laws of the Territory of Hawaii, hereinafter called the "Assignee,"

Witnesseth That:

In consideration of the sum of Ten Dollars ($10.00) lawful money of the United States of America, and other good and valuable consideration now paid to the Assignor by the Assignee, the receipt whereof the Assignor hereby acknowledges, the Assignor does hereby grant, bargain, sell, assign, transfer and set over unto the Assignee, its successors and assigns:

All that certain unrecorded lease dated March 1, 1940, by and between Hawaiian Transportation & Rock Products Company, Limited, as Lessor, and Roy Eaton, as Lessee, which said lease has been heretofore assigned to Nehi Beverage Company of Hawaii, and has been modified by letters of agreement dated January 24, 1941, and August 22, 1946, said lease being for a term to end May 31, 1950.

Exhibit No. 17—(Continued)

To Have and to Hold the same unto the Assignee, its successors and assigns, for the unexpired residue of the term of said lease.

And, for the consideration aforesaid, the assignor does hereby covenant with the Assignee, its successors and assigns, that the Assignor is the absolute owner of said lease, free and clear of and from all encumbrances; that the Assignor has good right to sell and assign the same as aforesaid, and that the Assignor will, and its successors and assigns shall, warrant and defend unto the Assignee, its successors and assigns forever, the said lease against the claims and demands of all persons claiming by, through or under said Assignor, provided, however, that said Bishop Trust Company, Limited, as Trustee aforesaid, shall not be liable under this covenant beyond its present interest in and to the proceeds from the sale of the assets and property of said special partnership.

And, in consideration of the foregoing assignment, the Assignee does hereby covenant, for itself and its successors and assigns, with the Assignor, its successors and assigns, to pay the rent reserved by said lease, and to observe and perform all of the lessee's covenants therein contained, and to indemnify and keep indemnified the Assignor, its successors and assigns, against the nonpayment of said rent or the breach of any of said covenants or of this covenant, and all claims, damages, costs, counsel fees and expenses in connection therewith.

Exhibit No. 17—(Continued)

In Witness Whereof, the parties hereto have executed these presents as of the day and year first above written.

NEHI BEVERAGE COMPANY
OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer.

NEHI BEVERAGE COMPANY
OF HAWAII,

By /s/ ROY EATON,
General Partner.

By BISHOP TRUST COMPANY,
LIMITED,
Trustee as Aforesaid.

By /s/ E. BENNER, JR.,
Its Vice President.

By /s/ G. H. VICARS, JR.,
Its Asst. Vice President.,
Special Partner.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the fore-

Exhibit No. 17—(Continued)

going instrument, and duly acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me appeared E. Benner, Jr., and G. H. Vicars, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Assistant Vice President, respectively, of Bishop Trust Company, Limited, Trustee under Deed of Trust made by Roy Eaton, Settlor, dated February 28, 1943, a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr., and G. H. Vicars, Jr., acknowledged said instrument to be the free act and deed of said corporation as Trustee as aforesaid.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judical Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Exhibit No. 17—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 7th day of November, 1946, before me appeared H. C. Lundburg and Kan Jung Luke, to me personally known, who, being by me duly sworn, did say that they are the President and Secretary-Treasurer, respectively, of Nehi Beverage Company of Hawaii, Ltd., a Hawaiian corporation, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation, and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said H. C. Lundburg and Kan Jung Luke acknowledged said instrument to be the free act and deed of said corporation.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

EXHIBIT No. 18

$91,000.00 Honolulu, T. H., October 1, 1946.

For Value Received, the undersigned, Nehi Beverage Company of Hawaii, Ltd., a Hawaiian corporation, promises to pay to the order of Roy Eaton in Honolulu, the sum of Ninety-One Thousand Dollars, payable in installments on the dates as indicated hereunder:

Oct. 1, 1947	$4,900.00	Apr. 1, 1953	$4,200.00
Apr. 1, 1948	4,200.00	Oct. 1, 1953	4,200.00
Oct. 1, 1948	4,200.00	Apr. 1, 1954	4,200.00
Apr. 1, 1949	4,200.00	Oct. 1, 1954	4,200.00
Oct. 1, 1949	4,200.00	Apr. 1, 1955	4,200.00
Apr. 1, 1950	4,200.00	Oct. 1, 1955	4,200.00
Oct. 1, 1950	4,200.00	Apr. 1, 1956	4,200.00
Apr. 1, 1951	4,200.00	Oct. 1, 1956	4,200.00
Oct. 1, 1951	4,200.00	Apr. 1, 1957	4,200.00
Apr. 1, 1952	4,200.00	Oct. 1, 1957	4,200.00
Oct. 1, 1952	4,200.00	Apr. 1, 1958	2,100.00

In case of default in any payment of any installment of principal or in the performance of the undertakings of the maker under pledge agreement of even date herewith, the entire debt shall immediately become due and payable at the option of the holder hereof, with interest thereon after maturity, at six per cent (6%) per annum. Should any suit for collection be instituted, the undersigned shall also pay costs of collection, including reasonable attorney's fees.

NEHI BEVERAGE COMPANY
OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer.

Secured by Pledge Agreement.

EXHIBIT No. 19

$24,500.00 Honolulu, T. H., October 1, 1946.

For Value Received, the undersigned, Nehi Beverage Company of Hawaii, Ltd., a Hawaiian cor-

poration, promises to pay to the order of Roy Eaton in Honolulu, the sum of Twenty-Four Thousand Five Hundred Dollars, payable in installments on the dates as indicated hereunder:

January 2, 1947, the sum of $21,000.00.

October 1, 1947, the sum of $3,500.00.

In case of default in any payment of any installment of principal or in the performance of the undertakings of the maker under pledge agreement of even date herewith, the entire debt shall immediately become due and payable at the option of the holder hereof, with interest thereon after maturity, at six per cent (6%) per annum. Should any suit for collection be instituted, the undersigned shall also pay costs of collection, including reasonable attorney's fees.

NEHI BEVERAGE COMPANY
OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer.

Secured by Pledge Agreement.

EXHIBIT No. 20

$39,000.00 Honolulu, T. H., October 1, 1946.

For Value Received, the undersigned, Nehi Beverage Company of Hawaii, Ltd., a Hawaiian corporation, promises to pay to the order of Bishop Trust Company, Limited, Trustee under Deed of

Trust made by Roy Eaton, Settlor, dated February 28, 1943, in Honolulu, the sum of Thirty-Nine Thousand Dollars, payable in installments on the dates as indicated hereunder:

Oct. 1, 1947	$2,100.00	Apr. 1, 1953	$1,800.00
Apr. 1, 1948	1,800.00	Oct. 1, 1953	1,800.00
Oct. 1, 1948	1,800.00	Apr. 1, 1954	1,800.00
Apr. 1, 1949	1,800.00	Oct. 1, 1954	1,800.00
Oct. 1, 1949	1,800.00	Apr. 1, 1955	1,800.00
Apr. 1, 1950	1,800.00	Oct. 1, 1955	1,800.00
Oct. 1, 1950	1,800.00	Apr. 1, 1956	1,800.00
Apr. 1, 1951	1,800.00	Oct. 1, 1956	1,800.00
Oct. 1, 1951	1,800.00	Apr. 1, 1957	1,800.00
Apr. 1, 1952	1,800.00	Oct. 1, 1957	1,800.00
Oct. 1, 1952	1,800.00	Apr. 1, 1958	900.00

In case of default in any payment of any installment of principal or in the performance of the undertakings of the maker under pledge agreement of even date herewith, the entire debt shall immediately become due and payable at the option of the holder hereof, with interest thereon after maturity, at six per cent (6%) per annum. Should any suit for collection be instituted, the undersigned shall also pay costs of collection, including reasonable attorneys' fees.

NEHI BEVERAGE COMPANY
OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer.

Secured by Pledge Agreement.

EXHIBIT No. 21

$10,500.00 Honolulu, T. H., October 1, 1946.

For Value Received, the undersigned, Nehi Beverage Company of Hawaii, Ltd., a Hawaiian corporation, promises to pay to the order of Bishop Trust Company, Limited, Trustee under Deed of Trust made by Roy Eaton, Settlor, dated February 28, 1943, in Honolulu, the sum of Ten Thousand Five Hundred Dollars, payable in installments on the dates as indicated hereunder:

January 2, 1947, the sum of $9,000.00.

October 1, 1947, the sum of $1,500.00.

In case of default in any payment of any installment of principal or in the performance of the undertakings of the maker under pledge agreement of even date herewith, the entire debt shall immediately become due and payable at the option of the holder hereof, with interest thereon after maturity, at six per cent (6%) per annum. Should any suit for collection be instituted, the undersigned shall also pay costs of collection, including reasonable attorney's fees.

NEHI BEVERAGE COMPANY
OF HAWAII, LTD.,

By /s/ H. C. LUNDBURG,
Its President.

By /s/ KAN JUNG LUKE,
Its Secretary-Treasurer.

Secured by Pledge Agreement.

EXHIBIT No. 22

In the Office of the Treasurer of the Territory of Hawaii

In the Matter of
The Special Partnership of NEHI BEVERAGE COMPANY OF HAWAII

CANCELLATION OF CERTIFICATE OF SPECIAL PARTNERSHIP

The Certificate of Special Partnership of Nehi Beverage Company of Hawaii heretofore filed in the Office of the Treasurer of the Territory of Hawaii is hereby cancelled as of the date of execution hereof.

The partners prior to the dissolution were Roy Eaton, General Partner, and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943, Special Partner.

In Witness Whereof said Roy Eaton and Bishop Trust Company, Limited, Trustee as aforesaid, have caused this Certificate to be executed this 10th day of December, 1946.

/s/ ROY EATON,
General Partner.

[Seal] BISHOP TRUST COMPANY, LIMITED,

By /s/ E. BENNER, JR.,
Its Vice President.

By /s/ CHAS. G. HEISER, JR.,
Its Vice President,

Trustee as Aforesaid and Not Individually, Special Partner.

Exhibit No. 22—(Continued)

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of December, 1946, before me personally appeared Roy Eaton, to me known to be the person described in and who executed the foregoing instrument, and acknowledged that he executed the same as his free act and deed.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

Territory of Hawaii,
City and County of Honolulu—ss.

On this 10th day of December, 1946, before me appeared E. Benner, Jr., and Chas. G. Heiser, Jr., to me personally known, who, being by me duly sworn, did say that they are the Vice President and Vice President, respectively, of Bishop Trust Company, Limited, a Hawaiian corporation, Trustee under Deed of Trust of Roy Eaton dated February 28, 1943; that the seal affixed to the foregoing instrument is the corporate seal of said corporation; and that the instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. Benner, Jr., and Chas. G. Heiser, Jr., acknowledged said instrument to be the free act and deed of said corporation as Trustee aforesaid.

[Seal] /s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires 6/30/49.

EXHIBIT No. 29

Roy Eaton Trust #1

Schedule of Income and Expenses

September 30, 1942 to September 30, 1950

	Fiscal Year Ended September 30,								
	1943	1944	1945	1946	1947	1948	1949	1950	Total
Income:									
Distributive share of partnership profits of Nehi Beverage Company for fiscal period ended June 30	$9,629.97								$ 9,629.97
Interest received on notes		$ 750.00	$750.00	$750.00	$547.91				2,797.91
Interest on bonds and savings and loan associations					276.17	$537.50	$545.28	$556.85	1,915.80
Dividends received on stocks				62.46	83.28	83.28	83.28	83.28	395.58
	$9,629.97	$ 750.00	$750.00	$812.46	$907.36	$620.78	$628.56	$640.13	$14,739.26
Expenses:									
Trustee fees		200.00	75.00	81.24	89.98	62.08	62.86	64.01	635.17
Tax service fees		15.00	25.00	25.00	25.00	15.00	15.00	15.00	135.00
Federal income taxes		2,131.71	794.82	81.96	197.36	111.55	73.89	75.51	3,466.80
Territorial income taxes		145.27	48.42		2.42				196.11
Interest accrued on bonds purchased					7.55				7.55
Bank charges					.15		.05	.05	.25
Postage on securities					1.67				1.67
		2,491.98	943.24	188.20	324.13	188.63	151.80	154.57	4,442.55
Net Income	$9,629.97	$(1,741.98)	$(193.24)	$624.26	$583.23	$432.15	$476.76	$485.56	$10,296.71
Gift by Roy Eaton at September 30, 1942									15,000.00
Trust Balance—Inventory attached									$25,296.71

EXHIBIT A

Nehi Beverage Company of Hawaii
Balance Sheet, September 30, 1946

ASSETS

Current Assets				
Cash in bank and on hand				$ 26,010.88
Accounts receivable, trade			8,777.76	
Accounts receivable, employees			73.65	
Claims receivable			243.13	9,094.54
Inventories, at the lower of cost or market				
Finished goods			2,078.99	
Bottles and cases			32,776.52	
Beverage coolers held for sale			787.48	
Manufacturing supplies			20,731.37	56,374.36
Special Deposit				25.00
		Depreciation		
Fixed Assets	Cost	Reserve	Net	
Beverage coolers	$ 725.25	$ 558.04	$ 167.21	
Machinery and equipment	67,575.78	33,267.05	34,308.73	
Automobiles and trucks	29,239.02	21,465.47	7,773.55	
Office furniture and fixtures	3,322.66	1,619.73	1,702.93	
Leasehold improvements	18,684.20	8,215.94	10,468.26	
	$119,546.91	$65,126.23		54,420.68
Deferred Charges				
Unexpired insurance			$ 3,476.88	
Repair parts, office supplies, etc.			3,500.26	
Prepaid taxes			836.94	7,814.08
				$153,739.54

LIABILITIES

Current Liabilities			
Accounts payable		$ 10,220.62	
Note payable, unsecured, Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton dated September 30, 1942, and accrued interest at 5% per annum		15,437.50	
Accrued taxes		2,250.83	
Accrued wages		316.90	$ 28,225.85
Partners' Capital and Drawing Accounts			
Special partner — Bishop Trust Company under Deed of Trust of Roy Eaton dated February 28, 1943			
Capital Account	$30,000.00		
Drawing Account	19,000.98	$49,000.98	
General Partner—Roy Eaton			
Capital Account	70,000.00		
Drawing Account	6,512.71	76,512.71	125,513.69
			$153,739.54

EXHIBIT No. 31

Roy Eaton Trust #1

Inventory of Assets
September 30, 1950

Cash		$ 377.61
Stocks: 100 shares Hawaiian Electric Co. "C," 4¼% cumulative pfd.		2,050.00
Bonds:		
U. S. Savings Bond—Series "G"	$5,000.00	
U. S. Treasury Bond, 2½	5,169.10	10,169.10
Savings and Loan Certificates:		
Home Mutual Savings and Loan Association	$5,000.00	
Citizens Federal Savings and Loan Association	5,000.00	
First Federal Savings and Loan Association of Hawaii	2,700.00	12,700.00
		$25,296.71

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EXHIBIT No. 32

Roy Eaton Trust #2

Schedule of Income and Expenses
February 28, 1943, to February 28, 1951, Inclusive

	Fiscal Year Ended February 28								
	1944	1945	1946	1947	1948	1949	1950	1951	Total
Income									
Distributive share of profits and losses of Nehi Beverage Co. of Hawaii for the fiscal period ending June 30	$7,722.93	$22,059.40	$23,076.92	$ 5,182.80					$ 58,042.05
Excess of assets received over investment on sale of Nehi Beverage Co. of Hawaii				40,034.70					40,034.70
Refunds					$ 171.29				171.29
Interest on bonds and savings and loan association					750.00	$ 811.56	$ 911.75	$ 947.92	3,421.23
Dividends received on stocks					890.00	966.45	1,197.67	1,579.13	4,633.25
Proceeds from sale of stock rights							2.26		2.26
	7,722.93	22,059.40	23,076.92	45,217.50	1,811.29	1,778.01	2,111.68	2,527.05	106,304.78
Expenses									
Trustee fees			850.00	300.00	144.80	154.46	177.66	206.89	1,833.81
Tax service fee		15.00	25.00	25.00	25.00	25.00	25.00	25.00	165.00
Federal income taxes		2,079.06	9,007.93	9,497.03		472.53	1,116.64		22,173.19
Territorial income taxes		147.44	494.00	308.47		39.31	134.76		1,123.98
C. and D. taxes on Mainland dividends					13.30	14.55	18.06	18.62	64.53
Bank charges				.05	.05		.05		.15
Postage on securities						2.46	.52		2.98
		2,241.50	10,376.93	10,130.55	183.15	708.31	1,472.69	250.51	25,363.64
Net income	$7,722.93	$19,817.90	$12,699.99	$35,086.95	$1,628.14	$1,069.70	$ 638.99	$2,276.54	$80,941.14
Gift by Roy Eaton at February 28, 1943									15,000.00
Trust balance—Inventory attached									$95,941.14

EXHIBIT No. 33

Roy Eaton Trust #2

Schedule of Receipts of Distributive Share of Income of
Nehi Beverage Co. of Hawaii

	Fiscal year ended June 30				June 30, 1946 to	
	1943	1944	1945	1946	September 30, 1946	Total
Distributive share of income	$7,722.93	$22,059.40	$23,076.92	$353.37	$4,829.43	$58,042.05
Payments made:						
April 1, 1944	600.00					
June 10, 1944	1,000.00					
June 30, 1944 (note)		16,400.00				
September 11, 1944	188.26					
October 11, 1944	30.00					
March 1, 1945	3,000.00					
June 13, 1945	2,634.67	300.00				
September 17, 1945		5,000.00				
March 8, 1946		359.40	2,140.60			
June 13, 1946			2,118.14			
September 13, 1946			5,000.00			
November 6, 1946			13,818.18	353.37	4,829.43	
	$7,722.93	$22,059.40	$23,076.92	$353.37	$4,829.43	$58,042.05

Note: By transfer of capital interest.

EXHIBIT No. 34

Roy Eaton Trust No. 2

Inventory of Assets, February 28, 1951

Cash		$ 3,604.22
Stocks		
27 shares American Telephone & Telegraph Co.	$4,409.40	
75 shares Chase National Bank	2,959.10	
75 shares Continental Insurance Co.	3,030.30	
60 shares E. I. duPont DeNemours & Co.	2,832.56	
50 shares Hawaiian Electric Co. "D," 5% Pfd.	1,017.50	
100 shares Hawaiian Electric Co. "E," 5% Pfd.	2,000.00	
55 shares Standard Oil Company of New Jersey	3,587.10	
60 shares F. W. Woolworth Co.	2,901.96	
300 shares Mutual Telephone Co. 4.8% Pfd.	3,099.00	25,836.92
Savings and Loan Certificates		
First Federal Savings and Loan Assoc. of Hawaii	$5,000.00	
Citizens Federal Savings and Loan Association	3,000.00	8,000.00
U. S. Savings Bonds—Series "G"		30,000.00
Note Receivable from Nehi Beverage Co. of Hawaii, Ltd.		28,500.00
		$95,941.14

EXHIBIT No. 35

Roy Eaton Trust No. 1—Schedule of Federal Fiduciary Tax Returns Filed

	Calendar Year								
	1942	1943	1944	1945	1946	1947	1948	1949	1950
Income									
Income from partnerships		$10,049.17							
Interest			$750.00	$750.00	$1,297.91	$379.32	$539.03	$550.00	$565.60
Dividends					85.29	85.00	85.00	85.00	85.00
Total Income	None	10,049.17	750.00	750.00	1,383.20	464.32	624.03	635.00	650.60
Deductions									
Taxes			193.69		1.72	4.14	1.72	1.72	1.72
Trustee fees		125.00	90.00	175.00	88.29	71.27	77.23	78.33	64.88
Contributions		176.67							
Bank charges						.15		.05	.05
Tax service fee									15.00
Total deductions	None	301.67	283.69	175.00	90.01	75.56	78.95	80.10	81.65
Income taxable to fiduciary	None	$ 9,747.50	$466.31	$575.00	$1,293.19	$388.76	$545.08	$554.90	$568.95
Tax paid	None	$ 2,842.28	$ 84.25	$109.25	$ 226.76	$ 54.86	$ 73.89	$ 75.51	$ 81.60

EXHIBIT No. 36

Roy Eaton Trust No. 2—Schedule of Federal Fiduciary Tax Returns Filed

	Calendar Year							
Income	1943	1944	1945	1946	1947	1948	1949	1950
Income from partnerships	$7,574.90	$22,916.42	$23,714.38	$ 446.06				
Interest					$ 750.00	$ 811.56	$ 886.75	$ 935.42
Dividends					755.00	987.25	1,166.80	1,300.91
Gain or (loss) from sale or exchange of capital assets	194.76		130.65	1,275.86	1,050.00	1,350.00	1,799.68	900.00
Refunds					171.29			
Total income	7,769.66	22,916.42	23,845.03	1,721.92	2,726.29	3,148.81	3,853.23	3,136.33
Deductions								
Taxes		147.44	494.00	308.47	8.00	18.40	78.54	102.24
Trustee Fees		415.00	325.00	475.00	175.50	165.98	198.48	186.07
Contributions	66.67	308.33	366.67	258.29				
Bank charges					.05	.05	.05	
Postage							2.46	
Tax service fee								25.00
Total deductions	66.67	870.77	1,185.67	1,041.76	183.55	184.43	279.53	313.31
Income Taxable to Fiduciary	$7,702.99	$22,045.65	$22,659.36	$ 680.16	$2,542.74	$2,964.38	$3,573.70	$2,823.02
Tax Paid	$2,079.06	$ 9,007.93	$ 9,386.80	$ 110.23	$ 472.53	$ 499.34	$ 617.30	$ 492.74

Filed at hearing June 18, 1951, T.C.U.S.

Before The Tax Court of The United States

Docket No. 24081

In the Matter of:

ROY EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Docket No. 24082

In the Matter of:

GENEVIEVE H. EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PROCEEDINGS

Pursuant to notice, the above entitled matter came on to be heard.

Before: Honorable C. R. Arundell,

Judge.

Appearances:

URBAN E. WILD, ESQ.,
MILTON CADES, ESQ.,

Appearing on behalf of Petitioners.

CHARLES W. NYQUIST, ESQ.,

Appearing on behalf of Respondent.

Honolulu, T. H., June 18, 1951

The Court: Well, I think I understand the matter generally so that I can follow it, and I think the best thing is to go ahead with the witnesses.

Mr. Wild: Mr. Eaton, will you please take the stand?

ROY EATON,

Petitioner, called as a witness in his own behalf, being first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Wild:

Q. Will you please state your full name?

A. Roy Eaton.

Q. Are you the petitioner in docket number 24081 now on trial? A. I am.

Q. And is the Genevieve Eaton referred to in docket number 24082 your wife? A. She is.

Q. When did you first acquire the franchise or three franchises for Nehi beverages?

A. Well, it was early in 1940. The business did not actually start operation until June of 1940, but before we made our investment in machinery and equipment, and so forth, we were assured we would receive the franchises if that was done. [24*]

Q. Prior to that time had Nehi Corporation had a franchise in Hawaii? A. No, they had not.

Q. And what were you to do in connection with that franchise if and when you received it?

A. Well, before they would agree to issue it to

*Page numbering appearing at top of page of original Reporter's Transcript of Record.

(Testimony of Roy Eaton.)

me I had to satisfy them that I had sufficient capital to go ahead and establish a bottling plant which would meet their specifications. That is, I had to buy bottling machinery, bottles, cases, crowns, and other supplies, trucks, and so forth, and be able to carry on the business of a Nehi bottler.

Q. And were there more than one of these franchises that you received?

A. Yes, there were three, one for each of the company's principal products, Royal Crown Cola, Nehi beverages and Par-T-Pak beverages.

Q. Prior to that time had you represented the company under a franchise of any sort?

A. No, sir, I had not.

Q. Was this your first experience as a professional bottler, as it were? A. Yes, it was.

Q. And did you have others in your employ who set up the machines, and so forth, to operate them? [25] A. Yes, I did.

Q. Now what time was it when you actually got the plant so that it could operate?

A. June 8, 1940, I believe was the first day we opened our business.

Q. And at that time who did you have employed in the plant and for what purposes?

A. You mean by name?

Q. No, no, your positions in the plant, let's put it that way.

A. We had a plant superintendent and bottle machine operators, five or six, and I think four

(Testimony of Roy Eaton.)

truck drivers to begin with, driver salesmen; a sales manager, office help, a janitor. I believe that comprises the principal ones.

Q. Now, will you describe the type of business that is done under this franchise? What did you do?

A. Well, we purchase concentrates from Nehi Corporation. With those concentrates we make syrup. That syrup, together with carbonated water is placed in bottles, cased and distributed to retail trade where it is sold to the public. We advertised our products to the public. That is the principal function of a bottler, I believe.

Q. Is capital an essential element in that business?

A. Yes, sir, the Nehi Corporation will not grant the franchise to anyone unless they are satisfied that they [26] have sufficient capital to conduct the business.

Q. And did anyone from Nehi Corporation come to Hawaii and assist you in setting up the bottling plant and other things?

A. Yes, they did. The Western Division Manager, who is in charge of the corporation's interest in that area, came down here when I came down here and assisted me in selecting the proper location and arranging the contract for the construction of the plant, and then he returned to the mainland while I continued to see about the purchase of the machinery and its installation. Approximately a week before the plant actually

(Testimony of Roy Eaton.)

started operation he came down here together with two other men who were in his employ to assist us in the opening of the business and to train me in its operation.

Q. Now you continued the operation of the business up until December 7, 1941, did you not?

A. Yes, sir.

Q. What effect did the enemy attack on December 7, 1941, have on your business, if any?

A. Well, of course, we didn't know right after December 7, we didn't know what was going to happen. However, the colonel in charge of the post exchanges contacted me and called me to his office and said that he wanted to know about the supplies that we had on hand and said that they [27] considered an adequate supply of carbonated beverages essential as a morale factor to the troops here and asked us what we could produce, and so forth. They indicated they would assist us in getting supplies. We did continue distributing our products to retail stores. We didn't know really from day to day just what was going to happen. We were very worried as to whether or not we were going to be able to obtain any supplies. It was very uncertain, except possibly for supplying our products to the military posts.

Q. Will you describe in general what was necessary at that time to receive supplies? Was it necessary to procure any orders of any sort?

A. Well, in the beginning, of course, the island was under military governorship, and it was neces-

(Testimony of Roy Eaton.)

sary to go to the military governor's office and obtain an order from him for shipping space. It was necessary then to send that to the mainland, and if and when such space was available in accordance with the priority which he had issued, those materials would move to the islands. Now that at first was conducted quite informally. Colonel Heyford, I believe, represented the territorial governor so far as the supplies were concerned, and he would call up the colonel in charge of the post exchange, for instance, and say that I was there in his office requesting space and that did he think that I ought to have it, did he think that my products [28] were necessary. He would say yes. He would give me some allocation of space.

Q. At that time were you advised when shipments were made? That is, shipments from the coast? A. No, we were not.

Q. And why was that, do you know?

A. Well, I think it was a question of security. All information about shipping was very closely guarded.

Q. And did you at that time have any concern about the franchise as it was in your own name, as you stated?

A. Yes, sir, I did. I was very much worried about it. Shortly after December 7 or on December 7, I was living on the other side of the island, and shortly after that it became very apparent it was going to be necessary for me to move over to the Honolulu side of the island because of gasoline

(Testimony of Roy Eaton.)

rationing, and time permitted because of the black out, and so forth. I moved over, if I remember, late in February. We hadn't been in our house but about a week when a bomb dropped up there on the hill where we lived and kicked dirt down on our house, which thoroughly frightened us, and from then on I began worrying a good deal about what would happen to the business should anything happen to me, especially as far as the franchises were concerned, because the franchises were really the greatest asset that we had, and they were issued in my name. If anything happened to me, why I didn't know what [29] would happen. I knew that it would be necessary for something to be done, but I didn't know what just exactly would happen under those circumstances.

Q. And you wrote some letters, which, your Honor, are Exhibits one, and the response two, and his letter in response three, and the letter in response four annexed to the stipulation. You wrote letters addressed to Nehi Corporation outlining your problem? A. That's right.

Q. Now what happened after you received the last letter which is dated here July 14, 1942?

A. Well, I wasn't at all satisfied with the suggestions made by the president of the Nehi Corporation as to the procedure that would be followed in case something happened to me. He indicated the possibility of sending a man down here. I knew he didn't understand the circumstances that existed here at the time, and I went to an attorney to seek

(Testimony of Roy Eaton.)

advice on what I could do to protect my family and those franchises in case anything happened to me.

Q. What were the circumstances that you just spoke of that would be different here? You said the changed circumstances from the mainland.

A. I believe in those letters the president of the Nehi Corporation stated that they would send a man to continue the operation of the plant and that it was the policy of [30] the Nehi Corporation to do everything possible to protect the heirs of any of their bottlers and see that the business continued and was either sold or a manager installed, or something to that effect. But that would not have been possible in Honolulu at that time, and there was no indication as to when it might become possible.

Q. Very well. Now you stated that you conferred with counsel on your problem. As a result of that, what did you finally decide to do?

A. Well, prior to the time that I had written these letters, actually I had been discussing this problem with Mr. Johnson and Mr. Prock.

Q. Who are they?

A. Mr. Johnson was my office manager. He started working for me, I believe, in the summer of 1941. Mr. Prock was in the insurance business here and was one of the first men that I met when I came to the islands, and Mr. and Mrs. Prock and myself and Mrs. Eaton had become very good friends. They were both in the service, but were stationed here. They had been in the reserves.

(Testimony of Roy Eaton.)

Their families had been sent to the mainland by the government.

Q. You say you conferred with them about your problem?

A. Well, they spent a good deal of time at our home after their families went to the mainland. Mr. Johnson, of course, having been associated with the business, was [31] actually continuing to do some work for me at that time in supervising the books, giving such time as he could, and both of them had been interested in the business, and Mr. Prock was also interested in our problems.

I knew that the Los Angeles plant, the Nehi plant was owned by two men and that both of their names were on their franchises, and I understood that was true in other places, and that was one of the ideas that we had discussed and one of the ideas that I brought up with my attorney when I went to see him.

Q. Had any suggestion been made concerning the possibility of the Nehi Corporation issuing a franchise to a corporation?

A. Well, I had been told very definitely they wouldn't. They would only issue their franchise to an individual or to two or three individuals.

Q. Now after all these conferences, what did you decide to do as your solution to your problem?

A. Well, I had two or three conferences with my attorney. He requested me to bring him copies of the franchises, which he went over and we discussed the problem generally, and it was his recom-

(Testimony of Roy Eaton.)

mendation that a partnership be formed, and we proceeded to do that.

Q. And what was the decision concerning the participation in that partnership by a trust?

A. Well, in our discussions one of the problems that came [32] up was the fact that while Mr. Johnson and Mr. Prock were now stationed here in the islands, it was possible that they might be leaving. In addition to that, neither one of them had had any experience in general business management, and it was my desire to have somebody associated, if possible, that would have broad experience in business management, and if something happened to me I would have further assurance that the business would be carried on to the best advantage for my family. Mr. Culbert, the president of the Nehi Corporation, had made some mention of an executor in one of his letters, and tying in a financial institution possibly or someone who could carry things on in case of my death.

Q. Well, as a result of these conferences and of your own ideas you executed the deed of trust and settled $15,000 and signed the partnership agreement, as is set forth in the stipulation?

A. I did.

Q. And at the time this partnership was formed, were there other general partners?

A. Yes, Mr. Johnson and Mr. Prock became general partners and their names were put on the franchise. That was very much a part of the whole

(Testimony of Roy Eaton.)

idea, an agreement to secure the franchise in case anything happened to me.

Q. And did you, after the formation of the partnership, [33] receive compensation for your services from the partnership? A. Yes, I did.

Q. And what was the amount of that compensation which you received at the start?

A. Well, at the start it was $1,250 a month.

Q. And how was that treated in connection with the partnership accounts?

A. Well, it was treated as a salary to me, as an expense of the business.

Q. I see. Do you yourself, as of those years, consider that as adequate compensation to pay you for your personal services to the business?

A. I did, yes.

Q. And later on was that salary modified?

A. Yes, it was. As our business increased and responsibilities became greater, my salary was increased to $1,750 a month.

Q. Now sometime in the early part of 1943 were you advised of some tax decision that might affect your position?

A. I was. My attorney called me on the phone and informed me that there had been a decision which would affect me and asked me to come down to his office, and he explained it to me, and I was naturally very much worried about it, because he said that there was a possibility that the tax on the [34] proportion of the profits which belonged to the trust might be assessed to me, and without it

(Testimony of Roy Eaton.)

being possible at all for me to get any of the income I would have been in a very bad way. I mean it wouldn't have been possible for me to pay the tax.

Q. Under the partnership agreement you could terminate the partnership on a sixty-day—with a sixty-day notice, as is shown in the stipulation. Did you consider that at that time?

A. Well, I wanted to carry the thing on the way it was. I mean the whole purpose of setting it up was again a protection for my family, and I didn't want to disturb that situation, and we had some discussions about it with the trust company, and the trust officers that had been administering it, and so forth, and with my attorney we went over it in quite some detail.

Q. And as a result of those conferences did you do anything?

A. Well, it was recommended and the trust company agreed to the establishment of another trust which would eliminate the provisions which might make this income taxable to me so that we could carry things on substantially as they had been carried on, and we followed out their recommendation. I did; I followed the recommendation.

Q. Now prior to the time that you were notified of this [35] decision of the court by your counsel, had you considered anything concerning your own tax problems as a motive for setting up the first trust or the partnership?

A. No, sir, I had not. The question of taxes was

(Testimony of Roy Eaton.)

never discussed in the establishment of the first trust and was never a consideration in any way.

Q. Now then, during the period of time that you were operating as a partnership, that is after the partnership was formed, what if any were your relations with Bishop Trust Company, Limited, who was the trustee named in the trust indenture and was your special partner as such trustee?

A. Well, I saw the trust officer who was in charge of the trust very regularly, and we discussed the problems of the business. There again I was interested in trying to educate them as to the operation of the business in case anything happened to me. I wanted them to know, and of course, all financial statements they saw, and any questions of policy or anything of that kind I discussed with them, and I think they were very well informed on the operation of the business, as far as its policies and finances were concerned.

Q. And how often would you say you would confer with them during that period of time?

A. At least once a month, and probably oftener.

Q. Did you seek their advice on various matters that came [36] up from time to time in the partnership business? A. I did.

Q. With whom did you deal in the Bishop Trust Company?

A. At first there was a Mr. White, and then very often Mr. Benner sat in with Mr. White on our discussions, and later on it was all Mr. Benner

(Testimony of Roy Eaton.)

practically altogether. That was quite later on in the arrangement.

Q. And what was their attitude in regard to the shares of the profit that were attributable to the trust interest in the partnership?

A. Well, one of the problems that the business faced was a very rapid expansion and inadequate capital, and we discussed that a good many times about leaving the profits in the business, and in fact it was necessary that we do it. One time we discussed the possibility of a bank loan and we decided against that, and it was determined to leave the profits in the business until such time as there was sufficient capital to pay them out.

Q. And during that period of time did the trust company or any officer press you on more than one occasion to know whether it was not possible to get portions of the profits at that time?

A. Well, they did. They, of course, required that enough of those profits be paid out to meet the expenses of the trust and taxes and that sort of thing, and that [37] was paid.

Q. And finally were all of the capital interests and all of the income interests of the trust paid to the trustee? A. Yes, sir, they were.

Q. Now coming up to the year 1946 there was a change made in your partnership in 1946. Will you explain that, please?

A. Well, after Mr. Prock and Mr. Johnson got out of the service they came back and became actively engaged in the business and remained so

(Testimony of Roy Eaton.)

for several months, and then because of certain personal problems and considerations they decided that they wanted to dispose of their interest in the partnership.

Q. Did you agree at that time with them to purchase their interest? A. Yes, I did.

Q. And I think that the bill of sale and all is in the stipulation.

A. We had a special audit made to determine the actual value of the partnership interest as determined by the books, and I purchased their partnership interest from them on that basis.

Q. And later that year was there some proposal made concerning the possible purchase of the partnership business?

A. Yes, there was. Three men, well one man came to me and talked to me about it. I believe it was sometime in [38] August.

Q. Of what year? A. Of 1946.

Q. And then you opened negotiations?

A. He expressed an interest in purchasing the plant.

Q. I see, and did you contact your special partner concerning that?

A. I did immediately, yes.

Q. And what happened as a result of that proposal?

A. Well, we entered into discussions with these people.

Q. When you say "we" who do you mean?

A. Well, I mean the trust company officers and

(Testimony of Roy Eaton.)

myself and then eventually we had a meeting with attorneys and the prospective purchasers and negotiated a deal, a sale.

Q. Did you have any personal interest in the purchasing company? A. None whatsoever.

Q. And the sale was finally agreed to by the special partner?

A. Yes, they participated in the negotiations at the time of the sale.

Q. And that sale was completed?

A. Yes, it was.

Q. And were the franchises transferred at that time? A. Yes, sir. [39]

Q. So that you had no further interest as owner of the franchises?

A. Absolutely. My name was taken off.

Q. However, who was the franchise transferred to? A. Who were they transferred to?

Q. Yes.

A. It was transferred to a Mr. Lundberg.

The Court: Is that by assignment on your part or by issuing new franchises by the Nehi Company?

The Witness: By the issuance of a new franchise. When you cease to have any interest in the business, the franchise is automatically cancelled, as far as I was concerned, and it was necessary for the Nehi Corporation to issue a new franchise then.

Q. (By Mr. Wild): And was the corporation named in that franchise as holder of it,

A. No, sir.

Q. Just the individuals?

(Testimony of Roy Eaton.)

A. That's right.

Mr. Wild: Your Honor, I think the copies of the notes and all, and the sales document are in the stipulation.

Q. Now during all this period of time of the special partnership were you giving accounts concerning the business and affairs of the company to your special partner? [40] A. Yes, sir.

Q. How often did you give those accounts to the special partner?

A. Well, our auditors were instructed to give copies of their financial reports to the trust company, and I always went down and we discussed them, and they were kept informed by me of the condition of the company in our regular meetings together.

Q. Who was this auditor? Was that an inside auditor with your company?

A. No, sir, that was the firm of Cameron and Johnstone.

Q. And they are independent auditors?

A. Certified Public Accountants, yes, sir.

Q. Now, during the period of this partnership, who supported your children?

A. I beg your pardon?

Q. During the period of this partnership, from what source did your children receive their support? A. From me, from my salary.

Q. And was that true during all of the years of the special partnership? A. Yes, sir, it was.

(Testimony of Roy Eaton.)

Q. So that no amounts were paid out by the trustee for the benefit of the children?

A. Never have been, no, sir. [41]

Mr. Wild: You may cross-examine.

Cross-Examination

By Mr. Nyquist:

Q. Mr. Eaton, you have testified at length concerning a franchise for the bottling of Nehi, Par-T-Pak and Royal Crown Cola. Is a franchise of that nature essential to the conduct of a bottled beverage business?

A. The Nehi business, it is, yes, sir, and the product that you bottle is the most valuable asset you have because of the national advertising and the assured quality of the products and the general reputation of the products.

Q. Well, is it practical to conduct a bottling business without such a franchise from some well-known, for some well-known beverage?

A. I don't think you can bottle any well-known beverage without a franchise. None of the nationally advertised beverages that I know about, Coca-Cola, Pepsi Cola, Nehi, Nesbitts, Delaware Punch, Hires, any of the beverages that I know anything about have parent companies and you have to have franchises and their permission and authority before you can bottle them.

Q. Then a franchise is really necessary to conduct a successful business in that line, is it?

A. I think it is, yes. There are a few instances,

(Testimony of Roy Eaton.)

I imagine, in the country where some entirely independent [42] bottler has been successful, but they are rather rare.

Q. It more or less represents the good will of the business, does it not, the name by which the product is known?

A. Well, yes, but it is a little more than that. I mean it is the—the parent companies employ rather high-powered talent to prepare advertising and merchandising plans which they make available to their bottlers, and so forth. There is a lot of assistance that they render.

The Court: May I ask, can you buy the concentrate unless you have a franchise?

The Witness: No, sir, you cannot.

The Court: Then a franchise is necessary to get the ingredients for this product?

The Witness: That's right.

The Court: That is what I thought.

Q. (By Mr. Nyquist): Well, you have testified concerning your concern over the possibility of your death and losing the franchise as a result of it. Did you consider that franchise to be an asset of substantial value to you or your estate?

A. Well, it was the greatest asset that my estate would have had.

Q. You mean that the physical equipment like the physical plant that you used to do the bottling, wouldn't that have a value by itself apart from the franchise? [43]

A. Yes, it would have a value. It could be sold

(Testimony of Roy Eaton.)

to someone, I presume, but it was the franchise that was the thing that is really worth the money and has the real value, the greatest value.

Q. Prior to the creation of the first trust in September of 1942, you operated the business as a sole proprietorship, did you not? A. Yes, sir.

Q. And did you have a business bank account?

A. Yes, sir.

Q. For the business as distinguished from a personal bank account? A. Yes, sir.

Q. You had both a business and a personal bank account? A. Yes, sir.

Q. At the time you created this number one trust what was the source of this $15,000 contribution to the number one trust?

A. I don't remember.

Q. Did you draw money from your business bank account? A. I don't remember.

Q. Did you draw money from your personal bank account?

A. I rather imagine I did. [44]

Q. Did you hand cash to the trustee?

A. No, sir.

Q. Did you give him your personal note?

A. No, sir.

Q. But you don't remember whether you drew the money from a business or a personal bank account?

A. No, sir, I don't. Of course, it was all mine, as far as that goes.

Q. And after the creation of the number one

(Testimony of Roy Eaton.)

trust, can you tell me what happened to that $15,000?

A. Well, the $15,000 was used by the trustee for the purchase of an interest in the partnership.

Q. Then it came back into the business, the $15,000 came back into the business, is that right?

A. Yes, sir.

Q. At the time you created the number one trust, was it your understanding that the income from that business that went into that trust would not be taxable to you?

A. The question of taxes never came up when we were discussing this matter. Frankly, I don't believe it was discussed at all. My sole interest was in establishing a set up which would protect my family in case anything happened to me.

Q. You mean it was a matter of indifference to you as to whether you or the trust paid the [46] taxes?

A. I don't think it came up. I don't think the question was discussed.

Q. You mean at that time it didn't occur to you as being a matter of importance one way or the other? A. That's right.

Q. What happened between then and the time of the creation of the number two trust that taxes suddenly loomed up so important and became a decisive factor?

A. Well, the first problem that came up, the first discussion we had was when my attorney called me and told me that because of some decision the in-

(Testimony of Roy Eaton.)

come which belonged to the trust might be taxable to me, and I couldn't ever receive any of that income. I didn't have any control over it or a thing, and I wouldn't have had the money to pay the taxes. It would have been ruinous if that had happened, and I was very much concerned about it.

Q. Then when you found out you might have to pay a tax on that income you reached the conclusion that you couldn't possibly operate under that method of doing business?

A. Not if that was the case.

Q. Why wasn't that circumstance involved when you created the number one trust?

A. I didn't know anything about the tax situation. It hadn't come up.

Q. Were you assuming that the number one trust was going [47] to pay the tax then?

A. I don't know what I was assuming, because the question of taxes hadn't come up at all. I was interested, as I say, in protecting my family's interest in case something happened to me, and my attorneys advised me that this was the best way to do it, and it seemed like a very logical way to do it, and we went ahead and did it. The question of taxes didn't come into it at all.

Q. Would you have created the number one trust if you had thought the taxes had to be paid by you?

A. No, of course, I wouldn't have.

Q. Then when you created it you assumed that income was not going to be taxable to you, is that correct?

(Testimony of Roy Eaton.)

A. I don't think I assumed anything about taxes. As I say, the question of taxes didn't come up.

Q. With whom did you consult, with what attorneys did you consult concerning the creation of that trust? A. With what attorneys?

Q. Yes.

A. I consulted with the firm of Smith, Wild, Beebe and Cades.

Q. Your present counsel in this proceeding?

A. That's right.

Q. You mentioned a Mr. Johnson and a Mr. Prock who were also general partners under the terms of the partnership [48] agreement dated September 30, 1942? A. Yes, sir.

Q. Exhibit 6 in this proceeding? A. Yes.

Q. How was the compensation of Mr. Johnson and Mr. Prock, how was their distributive share of partnership income to be determined?

A. Well, until such time as they were devoting their full time to the business.

Q. Yes.

A. Their percentage of the profits which they were to receive was to be restricted. Now just exactly how that was done, I don't remember.

Q. Well, I see a clause in here which I will read to you to refresh your recollection. (Reading): "Provided"—this is reading from page four of Exhibit 6. "Provided, however, that general partners Charles P. Johnson and/or Walter L. Prock, Jr., shall only be entitled to such amounts of the net profits of the business during any period in which the business of the partnership is not the principal

(Testimony of Roy Eaton.)

activity of said partners, a sum in excess of 12% per annum of the amount of said general partners' capital and interest." In other words, were you restricting their profits to 12% of their capital investment when they were not working in the [49] business?

A. I guess if that is what it says, that is what it was.

Q. Why should you so restrict their profits?

A. Well, because one of the things that I was interested in was having them become active in the business just as soon as they got out of the service, and I think they were so interested, too.

Q. But weren't they entitled to a fair return on their capital even if they were not working there?

A. Well, I think 12% would be a pretty fair return.

Q. You think 12% would be a pretty fair return on capital invested in the business?

A. Yes, sir.

Q. Still on the same subject of Mr. Prock and Mr. Johnson, I believe you purchased their interest some time in 1946, is that correct?

A. Yes, sir.

Q. At the time you purchased those interests did you pay for them the book value of the interests?

A. Yes, sir, we had a special audit made to determine that.

Q. Was the franchise carried as an asset on the books? A. No, sir.

Q. Was good will carried on the books?

A. I don't believe so.

(Testimony of Roy Eaton.)

Q. Who were these people who bought the business in 1946?

A. It was a Mr. Hal C. Lundberg, Mr. Harry Leong and Mr. [50] K. J. Luke.

Q. When did you start to negotiate with them for the sale of the business?

A. I believe it was in August.

Q. At that time was the franchise to bottle these three beverages, Nehi, Par-T-Pak and Royal Crown Cola standing in your name? A. Yes, sir.

Q. And when you sold the business did the buyer pay $135,000 approximately for that franchise?

A. No, sir.

Q. For the surrender of the franchise so that they could receive the franchise from the company?

A. Franchises cannot be bought and sold. They paid that for the good will of the business——

Q. For the good will of the business, but the good will was represented more or less by the franchise, was it not? There could be no good will without the franchise, let's put it that way.

A. That is true, I think; yes.

Q. The franchise stood in your name at that time? A. Yes, sir.

Q. And back in June, on June 30th when you bought the interest of Mr. Johnson and Mr. Prock, when you bought their partnership interests, you made no payment to them for good [51] will?

A. I believe the basis under which any interest in the partnership could be bought and sold was covered in the terms of the partnership agreement, and I think that was carried out absolutely. I think

(Testimony of Roy Eaton.)

that was all covered at the time the partnership papers were drawn up, so that in the event any one of the partners wanted to buy or sell, or in case of death of any one of the partners, I think all those things were covered in that agreement. They were carried out.

Q. That is, you made no payment for good will or the franchise to these partners that you bought out at that time?

A. I guess not. I mean as business it wasn't reflected in the books. It was done in accordance with the partnership agreement.

Q. The franchise was in your name and not in the partnership name, I suppose, wasn't it?

A. No, sir, the franchise was in the name of Johnson, Prock and Eaton.

Q. Johnson, Prock and Eaton?

A. Yes, sir, at the time, as long as they were in the partnership. That was a very important part of the whole set up.

Q. And after they left the partnership—— [52]

A. Then it automatically came in my name.

Q. At the beginning of your testimony you were discussing your motives or reasons for setting up this partnership, and I believe you stated you were afraid that something might happen to you.

A. That's right.

Q. And for that reason you created the partnership to take in other men so the franchise would not be held in your name alone, is that correct?

A. Yes, sir.

(Testimony of Roy Eaton.)

Q. That does not explain your reason for taking the trust into the partnership, does it?

A. Yes, sir, it does, because neither Mr. Prock nor Mr. Johnson had had any experience in the general management of a business. They had had not too much financial experience. Mr. Johnson was a bookkeeper, an office man. Mr. Prock was a salesman and had quite some experience in the selling field, and one of the primary reasons of the creation of the trust to become a partner was so that they would be there to advise and have a real reason and be required to be active in that business in case anything happened to me. And they were active before, as far as that goes, and I could educate them. Also there was the problem of Mr. Johnson and Mr. Prock being in the service, and while they were stationed here at that time, they might be moved away from here at [53] any time.

Q. Then you say that your purpose in taking the trust in was to get some experienced management personnel that could take over the management of the business in the event that you or Mr. Prock or Mr. Johnson were not available, is that it?

A. Yes.

The Court: I don't quite understand that. Do you mean officers of the Bishop Trust Company?

The Witness: Well, yes, sir. They certainly were very familiar with business conditions here in the Territory in the operation of the business. Before the trust was created I went down and talked with them, and they pointed out to me some of the busi-

(Testimony of Roy Eaton.)

nesses that they did have a finger in and were assisting in the management of, and so forth. I talked to them about what their charges would be and everything of that kind, and just exactly what would happen in case something happened to me, what they would do, and that was the reason that we got them into the picture, and it was felt advisable that they should be in the picture in case anything happened to me.

The Court: It is your testimony that you established this trust in order that the trustee would be in a position to enter into the actual management of your business if something happened to you? [54]

A. And through advising assist in it, yes, sir.

The Court: You could have done the same thing if you wanted by a testamentary trust, couldn't you?

The Witness: I don't know what that is.

The Court: One provided by your will.

The Witness: Well, I don't know. We discussed it. As I remember, the Nehi Corporation said something about an executor, but they wouldn't have known much about the business, and it would have been more difficult for them to do anything about it. We discussed that at quite some length before we went into it.

Q. (By Mr. Nyquist): Well, Mr. Eaton, on your death your 60% interest in the business would go to your executor——

A. I beg your pardon?

Q. In the event of your death your 60% interest

(Testimony of Roy Eaton.)

in the business would pass to your executor for him to dispose of pursuant to your will, would it not?

A. Yes, sir, I imagine it would.

Q. And that 60% would still be the controlling interest in the business, would it not?

A. Yes, and under the terms of my will the Bishop Trust Company was to be the executor of my estate, too, which would give them a further interest in the thing, for the protection of my family.

Q. But the Bishop Trust Company as trustee of either of [55] these trusts would have no control over the management and operation of the business either before or after your death, would it?

A. I think they very definitely would. I think if anybody mismanaged or did anything in that business that they felt was not sound business practice, I think they were very definitely in a position to step in and have their say on the matter. I think they could do it legally. It was certainly my understanding that they could.

Q. If that is the case, why did you put a provision in the trust indenture relieving them from responsibility from your acts that you did or consented to?

A. Well, I am not a lawyer, and there are several things in that trust which I think are required by the law under which the thing was created, and I read the thing over, of course, before we went into it, but I was advised that that would accomplish what I was interested in accomplishing and was the best way to accomplish it.

(Testimony of Roy Eaton.)

Mr. Wild: Might I just ask for my own information what page of the trust instrument counsel was referring to?

Mr. Nyquist: I haven't been able to locate it.

Mr. Wild: I haven't either.

Mr. Nyquist: It may be in the partnership agreement.

The Court: I thought the question was directed to the fact that the grantor had a control over investments. I [56] thought the question was directed to that.

Mr. Cades: If your Honor please, I do not believe that the provision referred to exist in the trust agreement. There is a provision that does relieve the trustee of liability for any loss resulting to the trustee but retaining any property in the trust that was given to the trust originally at the time of the creation of the trust.

The Court: I don't know what the form was, but the way it has been stated is that the corpus of the trust was $15,000.

Mr. Cades: Yes, sir.

The Court: Which would be money, and the trustee with the money buys an interest in the operating business. I don't know whether that is the form it took or whether in fact it was a grant of an interest in the operation of the business. I don't think it is of too much consequence.

Mr. Cades: It has been stipulated and testified to it was in cash which was directed to be used and was used for the purpose of purchasing the interest.

(Testimony of Roy Eaton.)

Mr. Nyquist: I read to you from paragraph K on page 7 of the trust instrument. (Reading): "The trustee may rely upon auditors' reports of the business or partnership known as the Nehi Beverage Company of Hawaii, and shall not be required to make any independent investigation into its affairs or accounts, and the trustee shall not be [57] answerable or accountable for any loss or damage resulting from any error of judgment or otherwise except through its own gross negligence or wilful default. Nor shall the trustee be answerable or accountable for any loss or damage resulting from any act consented to by the settlor, or for any loss or damage resulting from any investment in or loan or advance to the partnership known as the Nehi Beverage Company of Hawaii."

Q. (By Mr. Nyquist): With that provision in the instrument the trustee was empowered to rely upon your management of the business, was he not?

A. Well, it has been my experience in dealing with most financial institutions that they protect themselves pretty well in any dealings, and I imagine that was something required by them. I don't know.

Q. In other words, the trustee assumed no responsibility for any management of the business?

A. I don't think they would. I think they had gone as far as they could go in that.

Q. After the number one trust had sold its interest in the business to the number two trust for

(Testimony of Roy Eaton.)

$15,000 what did the number one trust do with that $15,000 that it received?

A. I believe they loaned it to the partnership.

Q. The partnership, the Nehi Beverage Company, the partnership we are talking about [58] here? A. That's right.

Q. And did the number one trust make other investments? A. I believe they did.

Q. Did the trustee consult with you before making such other investments?

A. The procedure of the trustee right along has been to make a recommendation of what they thought should be done, and without exception they have followed that recommendation.

Q. You mean they have made a recommendation and you have merely approved their recommendation, is that it?

A. That's right. That is just as a matter of form.

Q. You spoke about your attorneys calling you and informing you of some new court decision that might make the income of the number one trust taxable to you. Was that the same firm of attorneys you testified to that prepared the trust instrument for the number one trust? A. Yes, sir.

Q. And they also drew the number two trust instrument for you? A. Yes, sir.

Q. Did you have any other counsel than this one firm you mentioned? A. No, sir.

Q. Who made the decisions concerning the business, the [59] policies?

A. I was the general manager of the business

(Testimony of Roy Eaton.)

and took charge and assumed authority for all the detailed operations of the business. Any questions of policy and that sort of thing that were thought questionable I took up with the trust company.

Mr. Nyquist: I have no further questions.

Redirect Examination

By Mr. Wild:

Q. You testified that after you had purchased the interest of the other two general partners you got the franchise in your own name?

A. Yes, sir.

Q. Who were you holding it for?

A. For the partnership.

Q. And this loan that was made by trust number one to the partnership, which counsel just asked you about, was that repaid by the partnership?

A. Yes, sir; and interest payments were made regularly.

Q. And that was paid to the trustee of trust number one? A. That's right, yes, sir.

Mr. Wild: No further questions.

Recross-Examination

By Mr. Nyquist:

Q. You stated that after you purchased the interest of [60] Mr. Johnson and Mr. Prock and the franchise was reissued in your name you were holding it for the partnership. Did you execute any written document to that effect?

(Testimony of Roy Eaton.)

A. No, sir; there were never any documents before about who—never any question about it.

Q. There never have been any documents that you were holding the franchise for the partnership either before or after that sale? A. No, sir.

Mr. Cades: If your Honor please, I think that is a matter of legal conclusion and the documents in the stipulation show that all the rights, privileges and so forth of the business formerly carried on by Mr. Eaton were carried on by the partnership by the bill of sale. We can't expect the witness to understand the law involved.

The Court: Is that all, Mr. Nyquist?

Mr. Nyquist: That's all, your Honor.

The Court: Is that all?

Mr. Wild: Yes, your Honor.

The Court: Just step down.

(The witness was excused.)

The Court: I am going to take a short recess.

(Recess.)

Mr. Wild: Mr. Prock, will you take the [61] stand?

WALTER PROCK, JR.

called as a witness in behalf of the Petitioners, being first duly sworn, was examined and testified as follows:

The Clerk: State your name and address for the record, please.

The Witness: Walter Prock, Jr.

(Testimony of Walter Prock, Jr.)

The Clerk: Spell your last name, please.

The Witness: P-r-o-c-k. 5228 Apo Drive, Honolulu.

Direct Examination

By Mr. Wild:

Q. Mr. Prock, are you Walter Prock, Jr., that was formerly a general partner in the special partnership of Nehi Beverage Company of Hawaii?

A. I am.

Q. Are you acquainted with Mr. Eaton?

A. I am.

Q. Who preceded you on the witness stand?

A. Yes.

Q. Who was the third general partner?

A. Charles P. Johnson.

Q. How long have you known Mr. Johnson?

A. About 27 years.

Q. Where is he at present, if you know?

A. In Los Angeles.

Q. When did you first meet Mr. Eaton? [62]

A. Shortly after his arirval in Hawaii. I believe he came in the early part of 1940, between then and the month of June, the opening of the plant. I met him and solicited his insurance account. I was in the general insurance business here.

Q. And what is your special line of business over all? Is it of the selling or office type of business or what? A. I am a salesman.

Q. You were a salesman? A. Yes.

Q. Had you had any interest in the Nehi Corporation franchise for Hawaii?

(Testimony of Walter Prock, Jr.)

A. Yes, I had.

Q. Will you please state briefly what that was?

A. In the year 1939 on a trip to the mainland I became interested in starting a business in Hawaii, and the Nehi Beverage franchise appealed to me, and I made inquiries about it in Oklahoma City and talked with my good friend, Charles Johnson, about the possibility of our going into this business together in Hawaii. Neither of us had much capital and we were both to see what we could do about getting capital to put us in business. I wrote the Nehi Company and it was suggested that I contact Mr. George Silver, the West Coast manager of Nehi and talk to him about my problem, since Hawaii came under his jurisdiction. This I did, and [63] he outlined to me the capital requirements to open a plant in Hawaii.

Q. Then when Mr. Eaton came down here you say you made a contact with him to sell insurance? A. Yes.

Q. Did you get to know Mr. Eaton quite well?

A. Very well.

Q. Was there any discussion started about the possibility of your getting into the Nehi Company of Hawaii, the Nehi distributor of Hawaii?

A. In the early part of 1940?

Q. Yes.

A. I have no clear recollection of discussing it at that time.

Q. Well, when was the first time that you had

(Testimony of Walter Prock, Jr.)

a discussion with him about the possibility of getting into and working in the business?

A. Sometime after Mr. Johnson and I had been called into the service, and it undoubtedly came up in Mr. Eaton's home. We spent several evenings a week, quite often, at his home after our families had been evacuated.

Q. What was Mr. Johnson doing at that time prior to his going into the service?

A. He was office manager for the Nehi Beverage Company. [64]

Q. Working for Mr. Eaton's business?

A. That's right.

Q. Did he continue to render services before he became a partner and after he was called into the service here? A. Yes, sir, he did.

Q. And what were those services?

A. Supervision of the keeping of the records insofar as he had the time to do so, generally on weekends and nights.

Q. I see, but at that time were you able to give any of your time and attention to active participation in the business?

A. Until I became a partner I had no official connections other than my interest in the business. I gave no time then.

Q. After you became a general partner in the business what was your participation, if any, in the business? What were you supposed to do?

A. After I was out of the service?

Q. Yes.

(Testimony of Walter Prock, Jr.)

A. My title was sales manager. It was my job to sell the beverage.

Q. But while you were in the service was it possible for you to attend to that?

A. No, it was not.

Q. I see, so that during the period of time that you were [65] in service before you got out, you stated a moment ago that you and Mr. Johnson would call at Mr. Eaton's home on evenings and sometimes weekends. At that time did you participate in discussions concernings the operation of the business? A. Yes, I did.

Q. Now in your discussions concerning the operations of the business did you yourself take up anything with the special partner during the period of time you were in the army?

A. No, I did not.

Q. And why was that?

A. Well, Mr. Johnson and I were new partners, you might say, and we were quite satisfied with the way Mr. Eaton, who was the majority partner and general manager of the business, was conducting the business. He had established his relationships with the trust special partner, and we saw no reason to change that in any way.

Q. Well, wasn't there another element there? Where were you during the working hours of the day?

A. Well, I was in the Dillingham Building for four years.

Q. And you were occupied there full time?

(Testimony of Walter Prock, Jr.)

A. I was.

Q. On other governmental matters?

A. That's right. [66]

Q. Did you discuss with the other two general partners various matters that would be discussed with the special partner? A. Yes, we did.

Q. And how frequently would that occur?

Mr. Nyquist: Objection, your Honor. I move that last be stricken. He has testified he was not present at any of the discussions with the special partner, so he is not in a position to testify of his own knowledge whether he discussed it with the general partners, matters that had been discussed with the general partners.

Mr. Wild: No, I said matters to be discussed.

Mr. Nyquist: Well, that is different then.

The Court: Would you repeat the question now?

(The question was read by the reporter.)

The Court: Now what period was this, after you got out of the service?

The Witness: I am referring to the period I was in the service at this point. Is that not correct?

Mr. Wild: Yes, I was.

The Witness: While I was an officer in the United States Army.

The Court: Incidentally, when did you become a partner in this business?

The Witness: September 30, 1942. That was the effective date. [67]

Q. (By Mr. Wild): Now after you got out of service did you participate in some discussions with

(Testimony of Walter Prock, Jr.)

the special partner? A. No, I did not.

Q. You did not? A. No, sir.

Q. But did you, as prior thereto, discuss those matters with the other general partners before they were taken up with the special partner?

Mr. Nyquist: Objection to that. your Honor. He was not present. He does not know what was taken up.

Mr. Wild: No, before they were to be taken up.

Mr. Nyquist: That question carries an implication that they were taken up, and there has been no testimony on that point.

The Court: Overrule the objection.

A. Yes, I did.

Q. When did you get out of the service, by the way? A. December, 1945.

Q. And shortly thereafter you desired to enter into some other line of business, did you?

Mr. Nyquist: Your Honor, I object to the leading nature of this line of questions ask that counsel refrain from leading the witness.

Mr. Wild: I will withdraw the question. [68]

Q. (By Mr. Wild): What if anything happended to your interest in the partnership after you got out of the service?

A. Immediately that I got out of the service I went to work for the Nehi Beverage Company.

Q. Yes, then after that what did you do?

A. I was sales manager. My job was to sell the beverage.

Q. You were sales manager, and during that

(Testimony of Walter Prock, Jr.)

period of time you operated as sales manager of the partnership? A. That is correct.

Q. And for how long a period were you sales manager? A. Eight to nine months.

Q. And then you terminated your activities as sales manager for the partnership? A. I did.

Q. And you withdrew from the partnership?

A. I did.

Q. And about when was that, if you recollect?

A. Sometime in July of 1946, I think.

Q. I see. When you first became a partner in the partnership was there any general discussion concerning in whose name the franchise from Nehi would be held for the partnership?

A. Yes, there was.

Q. And what was that discussion?

A. Mr. Johnson and I knew that the franchises had to be [69] in the name of individuals, and along with Mr. Eaton's thoughts of providing for the event of his death that Mr. Johnson and I would continue the operation of the business and try to take care of his family problems along with our own, and it was agreed that by putting the franchises in the names of the three partners, in the event of the death of any one of the partners the other two could continue the operations quite satisfactorily.

Mr. Wild: You may cross-examine.

(Testimony of Walter Prock, Jr.)

Cross-Examination

By Mr. Nyquist:

Q. Over the period of years that the business was operated up to the time you sold your interest, the franchise had increased in value, had it not?

A. The franchise is not something you can sell, if you are speaking of money value.

Q. Let's word the guestion this way then: Over that period of time the Nehi Beverage Company of Hawaii had built up a relatively prosperous business, had it not? A. That is correct.

Q. And this was done through advertising and sales effort, was it not? A. It was.

Q. Therefore, the franchise was a valuable asset to whoever owned it, was it not? [70]

A. It was.

Q. At the time you sold your interest in the partnership you received an amount equal to the book value of the assets, did you not? The book value of your proportionate share of the assets, I should have said.

A. I believe that is correct.

Q. And that book value did not include any value for good will or franchise, did it?

A. That's right, it did not.

Q. So you received no payment by way of payment for any increase in good will or franchise value, did you? A. I did not.

Q. The franchise stood in your name as well as the names of the other two general partners?

(Testimony of Walter Prock, Jr.)

A. It did.

Q. But was that merely done as a matter of convenience in case of the death of Roy Eaton so that you would be able to continue the business in the event of the death of Roy Eaton?

A. No. It was done so that—Johnson and I made a decision that when we were out of the service we would be in the bottling business and make that our full time business, and we felt that it was certainly protecting our interest while we were in the service to have our names on that [71] franchise.

Q. I see.

A. Because, as a matter of fact, on the death of Mr. Eaton, Johnson and I would then own the franchise.

Q. But when you sold out you received nothing to compensate you for any interest you might have in the franchise, is that correct?

A. I believe it so states in the agreement.

The Court: Is the franchise an exhibit?

Mr. Wild: No, your Houor, it is not.

Mr. Cades: We do have copies available that we could submit.

The Court: I was wondering if it is a matter that runs from year to year. How does it run?

The Witness: It is a continuous instrument.

Mr. Wild: It is a continuous franchise, as I understand it.

The Court: But subject to withdrawal at the will of the Nehi Company, I suppose.

(Testimony of Walter Prock, Jr.)

Mr. Cades: That is correct.

Mr. Wild: It can be cancelled. We might as well put it in, your Honor, photosatic copies of them.

The Court: I don't care for all that. I was just trying to get some idea about it as the examination proceeds.

Mr. Wild: We might put in one, your Honor, as [72] illustrative of the others. The particular contract itself was not a point in issue. The particulars of the contract, or franchise, were not in issue in the cause.

The Court: Well, I am not interested in it either, Mr. Wild, but just exhibits in the nature of a right to operate.

Mr. Wild: It could be cancelled out.

The Court: Under this name and to acquire the ingredients and what not, and whether that is just at the will of the granting company. Now that is the way a lot of these franchises are, like a lot of these automobile ones. They can be taken away in a moment, but as a matter of practice they never are.

Mr. Cades: If your Honor would like, I could read a section directed to that.

Mr. Nyquist: If part of the instrument is going in, I would like to have the whole instrument in the record.

The Court: Well, I suppose you have a right to that. Well, let's pass it and you people look into it and see if it is needed.

(Testimony of Walter Prock, Jr.)

Mr. Cades: Your Honor, I would like to read this in.

The Court: Then the whole instrument will have to go in.

Mr. Cades: Yes, then we will offer the whole instrument. It says, (reading) "This license is of a personal [73] nature and may be transferred and assigned by the bottler only upon first obtaining written consent of the company and cannot under any circumstances be transferred to a corporation. It is further understood that said license should exist and continue only so long as the sale of Par-T-Pak beverages throughout such Territory is maintained in such volume and manner as is satisfactory and profitable to the bottler and to the company. It is therefore agreed that this license shall continue only at the unrestricted will of the parties thereto and may be terminated by either through service of written or personal notice upon the other."

The Court: Incidentally, does that purport to be an exclusive license for the Territory here?

Mr. Wild: Yes, your Honor.

The Court: Or could they grant a similar one to someone else?

Mr. Cades: No, this is exclusive. It is supposed to be exclusive. We do not have sufficient copies here to submit in evidence, but I would like to submit two. I would like to offer at this time photostatic copy of Par-T-Pak licensing contract granted to Roy Eaton dated March 18, 1940, and

(Testimony of Walter Prock, Jr.)

Par-T-Pak licensing contract granted to Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., dated October 6, 1942, with the stipulation that there were [74] two other similar, exactly similar franchises in the same names and at the same dates, covering Nehi Beverages and Royal Crown Cola. Is that agreeable?

Mr. Nyquist: If counsel can assure me that the terms of the franchises for the other two beverages were the same as the terms of this, I will so stipulate.

Mr. Wild: The special partner just tells me that they are different.

Mr. Nyquist: Your Honor, in view of the possibility that there are differences in the contract, I would agree with Mr. Cades if he wishes to put each of the contracts in, but I would not stipulate that the others were similar.

Mr. Cades: Then we are unable to furnish copies of these.

Mr. Nyquist: They can be put in with permission to withdraw for the purpose of making copies.

The Court: Put them in one at a time.

Mr. Cades: First I would like to offer Nehi licensing franchise granted to Roy Eaton granted March 18, 1940.

The Clerk: Exhibit 52.

The Court: It will be received.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 52.) [75]

(Testimony of Walter Prock, Jr.)

Mr. Cades: Royal Crown Cola agreement granted to Roy Eaton dated March 18, 1940.

The Clerk: Exhibit 53.

The Court: It will be received in evidence.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 53.)

Mr. Cades: Par-T-Pak licensing contract granted to Roy Eaton dated March 18, 1940.

The Clerk: Exhibit 54.

The Court: It will be received in evidence.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 54.)

Mr. Cades: Nehi licensing franchise granted to Roy Eaton, Charles Johnson and Walter Prock, Jr., dated October 6, 1942.

The Clerk: Exhibit 55.

The Court: It will be received in evidence.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 55.)

Mr. Cades: Royal Crown agreement granted to Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., dated October 6, 1942.

The Clerk: Exhibit 56.

The Court: It will be received in evidence. [76]

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 56.)

(Testimony of Walter Prock, Jr.)

Mr. Cades: Par-T-Pak licensing contract granted to Roy Eaton, Charles P. Johnson and Walter L. Prock, Jr., dated October 6, 1942.

The Clerk: Exhibit 57.

The Court: It will be received in evidence.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 57.)

The Court: Go ahead with the witness.

Q. (By Mr. Nyquist): Will you answer the question?

A. What was the question again?

Mr. Nyquist: Will you read the question, Mr. Reporter?

(The question and answer were read by the reporter as follows):

"Q. But when you sold out you received nothing to compensate you for any interest you might have in the franchise, is that correct?

"A. I believe it so states in the agreement."

Q. (By Mr. Nyquist): Will you answer the question directly? You said you believe it so states in the agreement. Do you believe that you received nothing to compensate you for any interest you might have in the franchise or good will of the business? [77] A. Yes.

The Court: Incidentally, what did you receive?

The Witness: My percentage.

(Testimony of Walter Prock, Jr.)

The Court: How much in dollars? Did you get it in cash?

The Witness: I had a check.

The Court: For how much?

The Witness: $2,050.00, I believe.

The Court: How much did you put in to start with?

The Witness: $2,500.00.

The Court: Didn't you get back as much as you put in?

The Witness: I did not.

The Court: Why was that? I thought the company was quite successful.

The Witness: Well, in 1946, business was dropping off at an alarming rate. The services had left the islands and it was not booming as it had previously.

Q. (By Mr. Nyquist): Did you ever have any agreement either written or oral with Mr. Eaton concerning the franchise, as to who would be entitled to any profits that might result from its increase in value?

A. I do not recall having any.

Mr. Nyquist: No further questions.

Mr. Wild: No redirect.

The Court: You are excused.

(The witness was excused.) [78]

EDWIN BENNER, JR.

called as a witness in behalf of the Petitioners, being first duly sworn, was examined and testified as follows:

The Clerk: State your name and address, please, for the record.

The Witness: Edwin Benner, Jr.

The Clerk: How do you spell your last name?

The Witness: B-e-n-n-e-r. I live at 4473 Aukai Street, Honolulu, T. H.

Direct Examination

By Mr. Wild:

Q. What is your present position, Mr. Benner?

A. I am Vice-President and Secretary of the Bishop Trust Company, Limited, and in charge of the trust department.

Q. How long have you been in charge of the trust department?

A. Since the spring of 1946.

Q. Prior to that time what was your position?

A. I was a trust officer of Bishop Trust Company.

Q. And for how long?

A. I joined the trust company in 1934, and I have been in the Trust department at all times.

Q. I take it that your active business life, so far as your own participation is concerned since 1931 has been with Bishop Trust Company, Limited?

A. That's right.

Q. What was the Bishop Trust Company's capital in 1940 and 1941, if you recollect? [79]

(Testimony of Edwin Benner, Jr.)

A. It was approximately $1,200,000, with a surplus of a like amount.

Q. And what type of business did it conduct at that time?

A. It conducted a trust company business here in the Territory. Banks do not do trust business and trust companies do not do banking business, and so during that entire time it was operated strictly as a professional fiduciary, with side issues such as insurance, real estate sales and brokerage, but its main business is administration of estates, trust, guardianships, agency accounts, acting as corporate trustee of all sorts and types, transfer agents, that type of business.

Q. In one fiduciary capacity or another do you have as part of your duties the management of various types of properties?

A. Yes, indeed.

Q. You might explain that.

A. The normal trust or estate that we handle, of course, consists primarily of stocks and bonds or ownerships in real estate, but very often we have the problem of the administration of proprietorships or own the control or total outstanding shares of businesses, and these change year for year as the estates are probated and closed out. Some of our trusts have operated business for many years, though. I can give you a few examples.

Q. I wish you would give me some examples of businesses that you have operated in a fiduciary capacity.

(Testimony of Edwin Benner, Jr.)

A. We have just closed up an estate that has as its principal [80] asset the controlling interest in a small structural steel company here in town with business operating right straight along. Our officer in charge was necessarily right on the job sometimes in the office, and so forth. We do own the controlling interest, through one of our fiduciary accounts, the largest specialty store, McInerny, Limited, that does $3,000,000 of business each year. I personally am secretary-treasurer of that company and sign all checks, incidentally. I received daily statements of its sales volume by department all the way through. We have a very active part.

Another business we are handling right now is the Honolulu Tile Business owned by the Worthington Estate. When Mr. Worthington passed away —it was his own business, and it was necessary that we step in and operate it, and not being familiar with that business we had some difficulty for several months and lost money until we were able to get things organized properly with an efficient manager, and are now pulling it out of the red and are doing very well. Our men in charge of that particular estate consult with me every week about their problems that they have there. They are on the job right along, too.

We have handled dairies; we have handled ranches; we have handled ice cream business. In 1944 and 1945 we administered the estate of Frances Wadsworth on the island of Maui. Mrs. Wadsworth at the time of her death was owner of [81] the

(Testimony of Edwin Benner, Jr.)

Maui Soda and Ice Works. That business owned the Coca-Cola franchise on the island of Maui. I made 18 trips to Maui during the year 1945 in connection with that business, taking a very active part in it.

The Court: Is that as executor?

The Witness: We were temporary administrators to start with, the license was issued in our name at first, and then to us as executor.

The Court: And what do you do there, try to liquidate the company as quickly as possible?

The Witness: We operated it just about a year. In 1944 and 1945 were boom years here in the islands because of the tremendous number of service people here, and bottling companies and business of that nature did a tremendous business, and rather than a liquidation program we continued to operate so that we would have a going business to sell to someone. We negotiated a sale eventually to a man who had been the West Coast agent for Coca-Cola. He was able to secure the consent of the Coca-Cola Company.

Mr. Nyquist: Objection, your Honor. I don't think there is any occasion to go into other bottling company cases.

The Court: We don't need to go any further on that.

Q. (By Mr. Wild): What other type of business?

A. I just jotted down a few, auto sales——

The Court: I think that is enough.

(Testimony of Edwin Benner, Jr.)

The Witness: We have the Ford agency in Hilo right [82] now that we are administrating.

Q. (By Mr. Wild): What, if anything, did you have to do with advising concerning policies, management, and so forth, of the Nehi Beverage Company of Hawaii?

A. Mr. White, who was the head of the Trust department in 1942, had his desk adjacent to mine. He handled my accounts when I was out of the office and I handled his. I eventually succeeded to his position. The handling of accounts went on even if the individual were here in town, not only when he was away on vacation, so when new accounts came in we met the parties involved as soon as possible so that we could carry on intelligently on any discussions that might come up. I believe I met Mr. Eaton at the time the document was signed, as I am one of the co-signers for the trust company. I can't put my finger on the exact date, but I met him at that time. I recall very definitely having numerous discussions with Mr. Eaton sitting at Mr. White's desk. It was just necessary to shift my chair around so I could join in with their conversations. And also with Mr. Eaton individually while Mr. White was not available.

These conversations were primarily about the need of retaining capital in the business due to the tremendous growth that this type of business was going through, and the advisability of our permitting a retention of earnings in the business so as to have a larger working capital. We [83] real-

(Testimony of Edwin Benner, Jr.)

ized that the franchise called for specifically serving this area adequately, and it meant that we had, the business had to grow as the demand required, and consequently we felt that it was the proper business venture, proper business to retain the money as was needed in the business for its growth, the purchase of new trucks, additional equipment for washing and bottling, inventorying. I know that accounts receivable, from my own knowledge, increased during that period, through the larger number of people being served. Our only insistance was that we be permitted to withdraw from the business sufficient to pay the taxes that were payable from the trust on account of its share of the income. That was handled by either telephone request to Mr. Eaton who would personally drop by with the check and would talk with us as to how business was going and our ideas of how long the army and navy was going to stay here, and developments of that nature.

Q. How often would you receive accounts of the business?

A. We received annual financial statements. We did not receive any interim accounts in writing. Mr. Eaton reported verbally as to how business was going, but we received these financial statements each year, and it was from these statements that we posted our books as to the distributive share of the income that we were entitled to receive. In other words, on the books of the trust on the ledger we put the journal entries that set up the amount dis-

(Testimony of Edwin Benner, Jr.)

tributable to us, and [84] then on the other side we would set up an amount that was being retained in the business as an account receivable by us from the business, in other words, the undistributed profit. We had to get it on our books because we were entitled to annual commissions, and it was required that we prepare annual accountings.

Q. How closely did you follow the operations of this Nehi Beverage Company of Hawaii?

A. Well, my contact in the detailed operations was more as to the growth of the business and the necessity for its growth, and what type of machinery was necessary to be purchased in order to permit the continued growth.

Q. Were you informed concerning the type of operations, the things that were done?

A. Yes, indeed.

Q. How frequently were inquiries made on that score?

A. Well, Mr. Eaton, I imagine, was in our office possibly every month. It is rather hard to recall, Mr. Wild, but frequently; definitely once every three months when he would bring in a check to help us pay our taxes. But he was a busy man and he didn't get uptown every day.

Q. Now at the time of the change over from trust number one to trust number two, did you participate at all in any of those transactions?

A. I believe I signed the trust instrument also. I did not [85] participate in any of the discussions.

(Testimony of Edwin Benner, Jr.)

Mr. White did. I knew about it because he talked with me for the trust company.

Q. You didn't participate in that?

A. No, but he and I made the joint decision on whatever was done, but I didn't talk to Mr. Eaton personally.

Q. That is at that time?

A. That's right.

Q. You advised with Mr. White as to what attitude the trust company had as special partner?

A. Yes, no one of us officers, even the senior trust officer, would take a step as receiving a new trust without consulting with some other trust officer or the management, which would be Mr. Damon at that time.

Q. Now when it came to the time of the offer to purchase the whole of the partnership business, were you personally consulted at that time?

A. I was. I had just returned——

Q. Do you recollect about what time of the year that was?

A. I definitely do. I had just returned from my first trip to the mainland after the war. I had come back the latter part of July. I had just taken over the active full time operation of these trusts. Mr. White had moved into the other position there for a year's temporary work, and I was the one that talked with Mr. Eaton and with Mr. Lundberg and the two Chinese gentlemen who became the eventual buyers. [86] I sat in on the discussions from the very start. I think Mr. Eaton came in and

(Testimony of Edwin Benner, Jr.)
talked to me about it before my meeting Mr. Lundberg or Mr. Luke and the other gentleman, and we had joint conferences and finally boiled things down, and Mr. Cades got into the picture, Mr. Milton Cades.

Q. And at that time were the various problems involved in the sale thoroughly discussed?

A. They were.

Q. And what did you do acting in your capacity as trustee of the trust that owned the special partnership?

A. Well, this partnership interest during 1946 and the latter part of 1945 had given us some concern. We had had some discussion as to the advisability of our continuing in it as business had fallen away. The war was over. The troops had been moved out. In 1946 up through the summer there we had suffered a loss, and I had talked it over with Mr. White before I went away—he with me rather—and in the spring of 1946 and when I came back the same picture existed, and when the opportunity came along for a sale we thought it was a very good thing to consummate and go ahead with. As long as the boom years of the war we felt it was a good business risk for this trust to have, but the picture changed and our ideas changed then too.

Q. So that did you act there in determining that you would join in the sale upon Mr. Eaton's suggestion or your own determination? [87]

A. Well, it is a little hard to say as to that par-

(Testimony of Edwin Benner, Jr.)

ticular sale. We were very much concerned about the interest in the partnership. We felt that it was no longer a suitable trust investment. If business was going to be on the declining side a sale to someone was indicated. We hadn't gotten to the point of actually talking it over with Mr. Eaton. Whether Mr. White did while I was away in the summer, I do not know, but when it came up Mr. Eaton said that there was a party interested, well we were interested, very definitely.

Q. But were you interested though because he told you or directed you to sell?

A. No, not at all. I just tried to tell you that it had given us some concern as an asset to have in a trust, and we were about to do something ourselves, to suggest that he buy us out or do something about getting out of that business. We didn't think it was a proper thing to continue to have in the trust.

Q. Now that sale was consummated, was it not?

A. Yes.

Q. And I believe the stipulation shows the copies of the instrument, the letter of offer, the acceptance and the assignment of the securities for the note.

A. They do. I was present when they were being considered and added as exhibits.

Q. Who at present holds the securities? [88]

A. The Bishop Trust Company does, as pledges.

Q. And for whom are you holding it?

A. They are pledged on notes to Mr. Eaton individually and to the Bishop Trust Company in a

(Testimony of Edwin Benner, Jr.)

fiduciary capacity as trustee. They are these notes and then the stock that the corporation has pledged by the owners of the stock as collateral on these notes, and we hold them in our vault.

Q. Is Mr. Eaton a director or officer or otherwise connected with the Bishop Trust Company, Limited?

A. No, I am the secretary, and I know that he is not a stockholder.

Mr. Wild: No further questions.

Cross-Examination

By Mr. Nyquist:

Q. Mr. Benner, you have testified concerning your advising with Mr. Eaton on the management of the business and the advisability of leaving or withdrawing trust profits from the partnership. I believe you mentioned one of the matters you considered was whether the armed forces were likely to remain in Honolulu in sufficient number to make the business continue to be profitable?

A. Yes.

Q. How did things look to you in about 1944 and early 1945 in that respect?

A. I think in June or July, 1944, the peak of the armed [89] forces contingent was here, as far as I have been able to gather at that time and since, both as to army and navy.

Q. But as to the future prospects, how did things look to you?

A. Well, we were still the staging area for the

(Testimony of Edwin Benner, Jr.)

advancement of our troops or navy forces across the Pacific, and while there had been some decline because the closer areas had been taken over, there still was a tremendous amount of business here.

Q. By early 1945 did things look on the decline?

A. Not particularly. The capitulation of Japan was not until the latter part of the summer of 1945, and I think it occurred rather suddenly to most of us. We hadn't expected it.

Q. You spoke about conferring with Mr. Eaton on the advisability of leaving profits in the business. Didn't that discussion really take more the slant of the need of the trust to get a little money out to pay taxes?

A. No, this was an investment, this interest in the partnership was an investment of this trust, and if we could produce more income for that trust, it was our job to do it as long as it was a proper business risk, and we considered the building up of that business so that the profits would be larger under the circumstances existing at that time was a proper business risk for us to take as trustee.

Q. Wasn't that also true of the number one trust?

A. The number one trust had sold its [90] interest.

Q. Yes, but wasn't it your job there to keep the money invested where it was profitably invested? A. Yes, sure.

Q. And yet you sold that out?

A. Yes, sure.

(Testimony of Edwin Benner, Jr.)

Q. How do you square that away with your duty to the number one trust?

A. Well, the remainder men in both trusts were the same. There was no change. We weren't doing anything to anybody at all for that sale.

Q. What was the reason for making the change, selling the assets from the number one trust to the number two trust?

A. It was agreed in the trust instrument that that is what we would do. I think it sets forth in the number two trust that we were to buy the interest in that partnership.

Q. Yes, but in your capacity as trustee of the number one trust, why did you sell your interest in the profitable partnership?

A. I tried to explain to you that there is no change in beneficial interests in the two trusts. Taxwise it was going to prove an advantage according to this decision that had been entered since the creation of that first trust.

Q. An advantage to whom?

A. To the Settlor, according to that decision.

Q. You spoke about your decisions to leave money in the [91] business. Did you consider that under the terms of the trust instrument you had the power to force the withdrawal of the profits from the business?

A. I think we could have without any trouble. we got money whenever we wanted it.

Q. Did you, during the period up to the time of the sale of the partnership to the corporation,

(Testimony of Edwin Benner, Jr.)

did you ever draw substantially in excess of what was necessary to pay taxes and administrative expenses of the trust?

A. I think our accounts have been stipulated here, how they were to be, and I didn't refresh my memory on that, sir.

Q. Let's put it this way then: When the time came that the trust would have a tax bill to meet, for example, didn't you usually have to make demand and sometimes repeated demands upon the partnership to get the funds to pay the taxes?

A. We would write a note or telephone, and sometimes if they didn't bring in the check, then a telephone call would go through. I think I testified a while ago Mr. Eaton didn't come uptown very frequently. He was a pretty busy man, and he would like to bring those checks in personally because that gave him another chance to talk with us.

Q. Did you go out to his place of business very often? A. No, never did.

Q. You have never been to the place of business?

A. No, when I took active charge of this account, we sold [92] it within three months.

Q. Was this the type of business that your company ordinarily would invest trust funds in?

A. No.

Q. Does your company ordinarily insist upon a provision in a trust instrument comparable to the provisions in these trust instruments relieving the trustee of all—saying, (reading) "That the trustee

(Testimony of Edwin Benner, Jr.)
shall not be accountable for any loss or damage, and so forth, resulting from any error of judgment of any kind except through its own negligence," and so forth—"Nor shall the trustee be answerable or accountable for any loss or damage from any act by the Settlor or loss or damage resulting from any loan or advance to the partnership," and so forth. Is that a typical provision in your trust instruments?

A. In instruments that deal with partnerships, yes. In instruments that deal with general assets put into a trust; inter vivos trusts, something like that, we ask for a release clause.

Q. Will you briefly explain to me the clerical mechanics in your office in handling a trust like this, the handling of its accounts and preparation of its tax returns?

A. Well, the books of account are, of course, all kept in our bookkeeping department, and disbursements are made by that department on the written request by requisition where [93] an ok'd bill of the officer in charge of the account. If there are journal entries to be put through, they will be by specific direction from him. Bear in mind we always have a substitute officer who can handle it, and his request is recognized. Accounts are prepared annually by the bookkeeping department, under the supervision of our head bookkeeper. They are typed and proofread and reviewed by the officer in charge and then again by the head of the trust department before they are sent out to the

(Testimony of Edwin Benner, Jr.)

beneficiaries, and they are sent out over the signature of the officer in charge of the account. They have a very careful procedure that must be followed, and it is the responsibility of myself now as being in charge of that department, to see that it is followed, and we do.

Q. And what reports and tax returns, and so forth, are prepared annually?

A. In some cases, and I believe it is true in this one, outside tax counsel is employed. I believe Cameron and Johnson prepared these returns. I am not certain, Mr. Nyquist, on that. We have a good tax department ourselves.

Q. If they did, would their fee be included in the fee you charge the trust?

A. No, we have a separate charge for tax purposes allowed under the statute. Allowances for extraordinary services are permitted. [94]

Q. But would that be included in the fee you would charge the trust?

A. It is shown in the account as a separate fee.

Q. Well, take for example, here is the fiduciary income tax return of the Roy Eaton Trust number two, which is exhibit 43. I see there you show on Schedule H a trustee's fee of $325. Would that include the cost of the preparation of such tax returns?

A. I can't answer that. I didn't prepare this return, and I can't tell whether he consolidated it or not.

(Testimony of Edwin Benner, Jr.)

Q. Well, is there any amount shown separately for the preparation? A. No.

Q. Would it ordinarily be included in that amount?

A. It ordinarily wouldn't show as part of the trustee's fee.

Q. Well, would you know whether this return was prepared——

A. It was prepared in our office.

Q. It was prepared in your office?

A. That's right.

Q. Then your fee included the cost of preparing that return, would it?

A. No, I can't answer that.

Q. Can you tell me generally then what is included in this $325 fee?

A. That would be our services agreed upon, our fee for our [95] services as trustee.

Q. That would be all these bookkeeping services, the reports you make? A. That's right.

Q. All the work you do, all these conferences you have, all this business advice? A. Yes.

Q. All included in this $325 fee?

A. That's right.

Q. Then a large part of the $325 would be for the clerical work, would it not?

A. No, there isn't very much clerical work, not in these particular ones, no.

Q. Well, do you have any idea how much time you would be spending on the other matters in connection with the trust?

(Testimony of Edwin Benner, Jr.)

A. That was a fee for that particular year. You will find that each year there was a different fee, and probably we were inadequately paid some years and very well paid in others for our time.

Q. But in those returns you didn't spend a large number of days personally on considering the matters of this trust?

A. We spent all the time that seemed required without any qualification whether we were going to make money on the job or not.

Q. You say you advised concerning business activities. Can [96] you tell me any specific advice you gave them?

A. Can I at this time recall some specific advice that I gave Mr. Eaton?

Q. Yes, concerning the management of that business? A. I am afraid I can't.

Q. Returning again to the matter of the transfer of the assets from the number one trust to the number two trust, the sale of the partnership interest—— A. Yes.

Q. Did you believe that the number one trust had a very favorable position from the tax point of view if it did not have to pay taxes on its income?

A. Yes, it probably did.

Q. Then why did you consent to the sale of the assets to the number two trust? Was it at Mr. Eaton's request?

A. This was in the spring of 1942, February. We then didn't know what was going to happen to the Islands, and I don't think the problem of the

(Testimony of Edwin Benner, Jr.)

taxes, the amount of taxes, dollarwise, was considered by us to be of too great a problem as far as our beneficiary was concerned.

Q. Well, did you have any reason for making the sale?

A. I have stated awhile ago that the beneficiaries of both these trusts were the same people.

Q. Yes, but I am asking whether you had any reason for selling the partnership interest in the number one trust to the [97] number two trust, as trustees of the number one trust?

A. Well, you see, the——

Q. Is your answer that you can't recollect any reason?

A. Possibly something like that. I don't remember the particular discussions on it.

The Court: Wasn't the reason rather obvious why it was done?

The Witness: At Mr. Eaton's request, to set up this new trust, and then that new trust called for the purchase of this. The partnership would have been dissolved if the change hadn't been made.

Q. (By Mr. Nyquist): Why do you say that?

A. Well, if it was going to affect Mr. Eaton in a way that he was going to be taxed on all the income that was going to be distributable to this trust, it was manifestly something that couldn't go on.

Q. Of what concern was it to the number one trust whether the partnership was dissolved?

A. He could dissolve it.

Q. He could dissolve it.

(Testimony of Edwin Benner, Jr.)

A. I think that the articles of partnership showed he could withdraw that, any partner could pull out. We didn't have that franchise.

Q. Would that have been a blow to the number one trust if he [98] had done that?

A. If he did nothing?

Q. If he had dissolved the partnership?

A. We would get back our $15,000.

Q. But you say he held the franchise personally?

A. For the account of the partnership.

Q. What do you mean for the account of the partnership?

A. No partnership can hold it. It has to be in the names of the individuals.

Q. Was there an agreement that he was holding it for the partnership in trust, any agreement about that?

A. I don't remember seeing any agreement.

Q. Do you recall any oral agreement?

A. Yes, in my conversations with Mr. Eaton——

Q. I am asking you whether you entered into an agreement or you were present when an agreement was made?

A. Not where we sat down and said, "You will do this and you will do that," no.

Q. Did you make investments for the trust, for either trust, other than the investments in the partnership business?

A. Yes, I think the accounts that we have filed here show.

(Testimony of Edwin Benner, Jr.)

Q. Were these investments made after the two trusts got out of the partnership business?

A. Unless I look at the accounts, I cannot answer that.

Q. When you made an investment or selected a security that [99] you thought was a favorable investment, would you secure the approval of Mr. Eaton before making the investment?

A. Yes. May I add a comment there about the policy of the trust company.

Q. No, I think your answer is sufficient.

The Court: I would like to hear it. Yes, make it.

The Witness: We would have secured Mr. Eaton's approval if there had been no requirement for approval. When there are settlors who have set up inter vivos trusts with us, it has been our policy as long as I can recall to propose investments and when the settlor is available to see whether he has any strenuous objections attached to them. We like to carry on in a manner that he is satisfied with. We have in our trust company a very carefully set up investment analysis department. We invest in certain securities that are approved in various trust companies. We work from the Bankers Trust Company list, and there are many securities that are approved, but you may have only one or two that would fit into a particular portfolio, and maybe the settlor doesn't like the name or something like that and we can suggest something else, but we have always made it a

(Testimony of Edwin Benner, Jr.)

policy, Mr. Nyquist, of proposing and asking their approval.

Q. But in this case, in addition to the policy, you regarded yourselves as obliged to do that under the terms of the trust instrument? [100]

A. The trust instrument said we always obtain his consent, so we did.

Q. That was for all the investments that you made? A. Yes, as I recall.

The Court: Is that a usual or unusual provision in these trusts?

The Witness: It is quite frequently found, from my experience, sir.

Q. (By Mr. Nyquist): Did you ever advise Mr. Eaton as to how much salary you thought he should draw from the business? A. No.

Q. Did he inform you as to how much salary he intended to withdraw from the business?

A. I knew what he was getting when the business was in operation in the early years. It was discussed, I mean just by way of conversation. We were advised formally by the partners when the general partners increased his salary to $1,750. As required, they advised us.

Q. But that was a matter where the decision was made by the general partners? A. Yes.

Q. Or the holder of the majority interest, or among the general partners and you did not participate in the decision?

A. We did not participate in it. We didn't ob-

(Testimony of Edwin Benner, Jr.)

ject to it. We felt that he was earning it and a proper salary for services [101] rendered.

Mr. Nyquist: I have no further questions.

The Court: Anything further?

Redirect Examination

By Mr. Wild:

Q. Did you consider the salary, did I understand you to say that you considered it an adequate compensation for his services in those times?

A. Yes.

Mr. Wild: No further redirect.

Mr. Nyquist: No further questions.

The Court: All right, step down.

(The witness was excused.)

Mr. Wild: The petitioner rests, your Honor, subject, however, to furnishing the exhibits. We haven't the photostatic copies of the return which give all the figures that have been inquired about, and also the photostatic copies of the franchises. We would like to withdraw those to get other copies made.

The Court: Very well, that may be permitted. Have you anything further?

Mr. Nyquist: Respondent rests, your Honor.

The Court: Well, we will conclude the record so far as taking the testimony is concerned. [102]

[Title of Tax Court and Cause.]

Docket Nos. 24081, 24082

MEMORANDUM FINDINGS OF FACT AND OPINION

Successive trusts for the benefit of the petitioner's minor children were created by the husband-petitioner. Under the first trust the income could be used by the trustee for the benefit of the children; under the second it could not be so used. Both were to endure until the youngest child became 25, when corpus and accumulated income were to be distributed to the beneficiaries; a trust company was the trustee; the trusts became special partners in a partnership in which the settlor was a general partner and made capital contributions of the corpus paid in by the settlor; both trusts were irrevocable.

Held, that the settlor did not have sufficient control over the trusts to make the income taxable to him. Helvering vs. Clifford, 309 U. S. 331, distinguished.

Held, further, that the trusts were bona fide partners in the partnership and their distributive shares of partnership income are not income of the petitioners.

Milton Cades, Esq., and Urban E. Wild, Esq., for the petitioners.

Charles W. Nyquist Esq., for the respondent.

The respondent determined deficiencies in income tax for the years and in the amounts as follows:

Year	RoyEaton	Genevieve Eaton
1943	$ 7,477.24	0.00
1944	23,589.24	0.00
1945	19,282.01	$381.09
1946	449.81	449.81

The principal issue is whether the income reported by two successive trusts created by the petitioner Roy Eaton for his minor children is income of the petitioners. The larger part of the income reported by the trusts was reported as their distributive shares of income of a partnership of which the petitioner Roy Eaton was a member. They also reported income from investments. As to both kinds of income the question is whether the settlor of the trusts had sufficient control over them so as to make their income taxable to him. As to the partnership income, there is a further question as to whether the trusts were bona-fide partners in a partnership in which the petitioner Roy Eaton was a member.

Issues as to net operating losses incurred in the operation of a sampan and a capital gain on the sale thereof were settled by stipulation.

Findings of Fact

At all times material hereto, the petitioners were husband and wife and were residents of the Territory of Hawaii or of the State of California. Their income tax returns were filed with the Collector of Internal Revenue for the District of Hawaii.

The petitioners have three children who in 1942

were respectively of the ages of 12, 10, and 8 years.

On March 18, 1940, the petitioner Roy Eaton, hereinafter called the petitioner, acquired franchises from Nehi Corporation to manufacture and sell three Nehi beverages* in the Hawaiian Islands. All three franchises provided that they were of a personal nature, and contained restrictions against any assignment, and prohibitions against assignment to corporations.

The petitioner had not had any previous experience in the bottling business. He commenced the operation of a bottling plant in Hawaii on June 8, 1940. The business conducted under the Nehi franchises consisted of the purchase of concentrates from Nehi Corporation, from which syrups were made. The syrups with carbonated water were bottled and the bottles were cased and delivered to the retail trade for sale to the public. The business required substantial capital for the acquisition of a plant, bottling machinery, and delivery equipment.

The attack on Pearl Harbor on December 7, 1941, and the subsequent military activities caused the petitioner considerable concern as to whether he would be able to obtain supplies to carry on his bottling business, and also as to whether the business would be continued in the event that anything happened to him in view of the fact that the franchises were in his name. Military authorities in Hawaii considered the maintenance of adequate

*The beverages were known by the trade names of "Nehi," "Royal Crown," and "Par-T-Pak."

supplies of carbonated beverages to be necessary for troop morale purposes and assisted the petitioner in obtaining shipping space for supplies for his business.

The petitioner corresponded with Nehi Corporation in 1942 and asked for suggestions as to what might be done with his franchises in the event of his death to insure that the business might be continued for the benefit of his wife and children. He was particularly concerned about providing for his family as he had put into the business everything that he had. The replies that he received from Nehi Corporation contained some suggestions but they were not satisfactory to the petitioner. The petitioner then consulted an attorney as to possible methods of keeping the franchises and continuing the business as a protection for his family.

The method decided upon and carried out was to organize a special partnership to operate the business, with a trust as a special partner. On September 30, 1942, a special partnership was organized in which the petitioner, Charles P. Johnson, and Walter L. Prock, Jr., were the general partners, and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton was the special partner. Johnson and Prock were acquaintances of the petitioner, and Johnson had been office manager of the petitioner's business. Both were in the military service at that time, but stationed in Hawaii. The petitioner was aware that Nehi franchises had been issued in the names of several individuals in other instances, and he felt that

having his franchises in the names of three persons would be some assurance of the continuance of the business in the event of his death. Neither Johnson nor Prock had had any experience in general business management, and the petitioner felt that it was desirable to have an associate in the business who had had such experience. The Bishop Trust Company, Limited, as a fiduciary, was experienced in the management of businesses, and that fact prompted the petitioner to admit it, as trustee, to the partnership as a special partner. The partnership was known as Nehi Beverage Company of Hawaii. It complied with all required legal formalities, such as filing for record and publication.

On the same date, September 30, 1942, the petitioner created a trust, herein called Trust No. 1, by executing a deed of trust naming Bishop Trust Company, Limited, as trustee. The petitioner paid over to the trust the sum of $15,000, which the trustee was required by the terms of the trust deed to contribute, as special partner, to the capital of the partnership for a 30 per cent interest therein. The trust was to endure until the youngest of the petitioner's children attained the age of 25 years, or until the prior death of the last survivor of the children. Upon termination, the corpus and accumulated income were to be paid over to the surviving children and the children of any deceased children and, if none, then to the persons other than the petitioner who would be the heirs-at-law of the last survivor of the children. In the event the partnership, Nehi Beverage Company, terminated dur-

ing the continuance of the trust, the trustee could terminate the trust and distribute to the beneficiaries.

During the continuance of the trust, the trustee was required to accumulate the income, but it was given discretion to use a part of the income for the maintenance, support, and education of the beneficiaries, and if income was not sufficient it could use corpus for that purpose. The petitioner reserved the right to convey additional property to the trustee. If any beneficiary was a minor when it became entitled to any distribution, the trustee could make payment to the parents or guardian of the minor.

The trustee was given the usual trust powers of management, sale, investment and reinvestment, with a provision that during the lifetime of the petitioner the trustee should obtain his consent to the making of investments and upon his death the trustee was to be restricted to investments that trustees are permitted by law to make. There was a further provision that the trustee might make advances or loans to, or further investments in the partnership Nehi Beverage Company of Hawaii "without liability for any losses resulting therefrom."

The trust, by its terms, was "irrevocable by the Settlor," and the settlor reserved the right to amend only by adding other property to the trust. It was further provided that in no event should any of the trust property or income be paid to or inure to the benefit of the petitioner.

The trustee was authorized to rely on the auditor's reports as to the business of the partnership, Nehi Beverage Company of Hawaii, and was not required to make any independent investigation into its affairs or accounts. The trustee was not accountable for any loss resulting from any act consented to by the petitioner or for any loss resulting from any investment in or loan or advance to Nehi Beverage Company of Hawaii.

The purpose of the special partnership was to acquire the assets and carry on the bottling business theretofore carried on by the petitioner. The capital provided for and the interests of the partners were as follows:

	Amount	Interest
Roy Eaton	$30,000	60%
Charles P. Johnson	2,500	5%
Walter L. Prock, Jr.	2,500	5%
Bishop Trust Company, Limited	15,000	30%
Totals	$50,000	100%

The special partner was not to be liable for the debts of the partnership beyond the extent set forth in a specified section of the Revised Laws of Hawaii.

The agreement provided that the general partners who were active in the business should receive as compensation for their services a salary chargeable as an expense in computing partnership profits in such amount as should be determined by the general partner or partners. The remaining net profits

and the losses were to be shared by all of the partners in accordance with the capital contribution of each, but with a limitation on the shares of profits of Johnson and Prock while they were not devoting full time to the business. Profits could be withdrawn at such times as the general partners determined. Only general partners had authority to transact the business of the partnership and incur obligations. The special partner could investigate the partnership affairs and advise the general partners as to its management. The determination by the general partner or partners owning the majority in interest of the capital contributed by the general partners was to be binding upon and establish the policy of the partnership.

Books were to be audited periodically, and a general account of partnership affairs was to be taken annually.

The partnership was to continue for 10 years and thereafter from year to year until terminated by any general partner giving six months' notice of intention to terminate. It could be terminated at any time on two months' written notice by a majority in interest of the general partners.

By bill of sale made as of the close of business on September 30, 1942, the petitioner conveyed to the partnership the assets used in his bottling business, and the partnership assumed his liabilities in connection therewith. The assets were listed at $106,960.55, and the liabilities at $76,960.55, leaving a net worth of $30,000.

Under date of October 6, 1942, Nehi Corporation

issued beverage franchises in the names of the three individuals who were the general partners.

Upon formation of the partnership, the petitioner drew from it a salary of $1,250 a month, which was later increased to $1,750.

Early in 1943, the petitioner Roy Eaton was advised by his attorney that under a recent court decision* he might be subject to income tax upon the trust's share of the partnership profits, without it being possible for him to get any of that income to use to pay the tax. The petitioner would not have been able to pay the tax from his own resources.

In order to meet the situation created by the court decision, the petitioner, on February 28, 1943, created a new trust, herein sometimes called Trust No. 2, with Bishop Trust Company, Limited, as trustee, with his children as beneficiaries. This trust was essentially the same as Trust No. 1, except that it did not contain any provisions for the use of either income or corpus for the education, support, or maintenance of the children during the existence of the trust. The trustee was to accumulate all income during the existence of the trust.

The petitioner contributed $15,000 to Trust No. 2, which sum was used by it to purchase from Trust No. 1 all of its right, title and interest in and to its 30 per cent capital interest in the special partnership. Formal instruments were executed assigning the partnership interest and amending the

*Helvering v. Stuart, 317 U. S. 154.

agreement of special partnership to show the new trust as being a partner.

On the same day, February 28, 1943, Trust No. 1 loaned the sum of $15,000 to the partnership and received from the partnership its note due one year after demand, with interest at 5 per cent per annum. Interest was paid periodically and the note was paid in full on November 23, 1946.

The trustee consented to the creation of Trust No. 2 and the sale of the property of Trust No. 1 to Trust No. 2 because there was no change in the identities of the persons in interest, and because it then appeared that there would be some advantage tax-wise.

During the existence of the special partnership, the petitioner Roy Eaton regularly discussed the policies and finances of the business with officers of the trustee. In the early years of the partnership, it was faced with a rapid expansion of its business and it had inadequate capital. The expansion of the business was largely due to the increase in military personnel in Hawaii during World War II. Under the Nehi franchises, it was necessary that customers be given adequate service. This necessitated that the partnership's facilities and equipment be enlarged, and required additional working capital. In order to provide additional capital, the partners and trust company officers agreed that until the partnership capital should exceed $100,000 no partner should withdraw any profits or capital except to pay taxes, commissions, fees and expenses of the special partner and taxes on the partnership profits of the general partners.

When partners Johnson and Prock were released

from military service they became active in the partnership business. In 1946, the partnership business was falling off and they decided to sell their interests. An audit was made to determine the values of their interests and the petitioner Roy Eaton purchased their interests at those values on June 30, 1946. The amounts that Johnson and Prock received did not include any sums for their interests in the franchises. Thereafter, an appropriate certificate of change of special partnership was filed in the proper public office and a notice was duly published.

The partnership, Nehi Beverage Company of Hawaii sold all of its assets and property to Nehi Beverage Company of Hawaii, Limited, as of the opening of business on October 1, 1946. The capital and drawing accounts of the special partner at the time of sale were, respectively, $30,000 and $19,000. The capital and drawing accounts of the general partner were, respectively, $70,000 and $6,512.71. The purchaser was a corporation in which the petitioner had no interest.

Notes were given by the purchaser in the aggregate amount of $165,000 for part of the purchase price, of which notes in the principal amount of $115,500 were payable to the petitioner Roy Eaton, and notes in the principal amount of $49,500 were payable to the Bishop Trust Company, trustee of Trust No. 2.

Appropriate steps were thereafter taken to dissolve the special partnership and cancel its certificate.

The distributive share of partnership income of Trust No. 1 for the period ended February 28, 1943, was $10,049.17. In succeeding years its income consisted of interest and dividends from investments. At September 30, 1950, the assets of Trust No. 1 consisted of cash in the amount of $377.61, and stocks, bonds and savings and loan certificates with a cost of $24,919.10, a total of $25,296.71.

The distributive share of partnership income of Trust No. 2 for years ended June 30, was as follows:

1944	$ 7,722.93
1945	22,059.40
1946	23,076.92
1947	5,182.80

Trust No. 2 realized a profit on the sale of partnership assets. In succeeding years its income consisted of interest and dividends from investments. At February 28, 1951, the assets of Trust No. 2 consisted of cash in the amount of $3,604.22 and stocks, bonds and savings and loan certificates with a cost of $92,336.92, a total of $95,941.14.

Trusts Nos. 1 and 2 duly filed Federal fiduciary income tax returns each year and paid the tax shown to be due thereon.

None of the funds of Trusts Nos. 1 and 2 was ever paid out to the beneficiaries thereof. During the period of the existence of the special partnership, the petitioner Roy Eaton supported his children from his own income.

The petitioner Roy Eaton, Charles P. Johnson, Walter L. Prock, Jr., and Trusts Nos. 1 and 2 really and truly intended to and did join together for the purpose of carrying on a business and sharing its profits and losses.

Trusts Nos. 1 and 2 were bona fide trusts for the benefit of the children of the petitioners, and the petitioners had no substantial control over, or interest in, the corpus or income thereof.

Opinion

Arundell, Judge: The issue for decision here is the same as that in the cases of Edward D. Sultan, et al., 18 T. C. . . ., and Thomas H. Brodhead, et al., 18 T. C. . . . That issue is whether income reported by trusts created by the petitioner Roy Eaton is income of Eaton and his wife either under the rationale of Helvering vs. Clifford, 309 U. S. 331, or on the ground that the trusts were not bona fide partners of Roy Eaton in the operation of a business.

The basic facts in these cases are essentially the same as those in the Sultan and Brodhead cases, supra. They require the same decision, namely, that the income reported by the trusts was their income, and that the respondent erred in treating such income as income of the petitioners.

Decisions will be entered under Rule 50.

Entered July 9, 1952.
Served July 9, 1952.
Received June 27, 1952. T.C.U.S.

The Tax Court of the United States, Washington

Docket No. 24081

ROY EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court entered July 9, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioner herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax for the taxable year 1943 in the amount of $4.93, and that there are no deficiencies in income tax for the taxable years 1944, 1945, and 1946.

/s/ C. R. ARUNDELL,
Judge.

Entered: Oct. 31, 1952.

Served: Nov. 3, 1952.

The Tax Court of the Unites States, Washington

Docket No. 24082

GENEVIEVE H. EATON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Memorandum Findings of Fact and Opinion of the Court entered July 9, 1952, the respondent herein, on October 9, 1952, filed a recomputation for entry of decision, and the petitioner herein, on October 30, 1952, filed an acquiescence in the respondent's recomputation. Wherefore, it is

Ordered and Decided: That there are no deficiencies or overpayments due in income tax for the taxable years 1945 and 1946.

/s/ C. R. ARUNDELL,
Judge.

Entered: Oct. 31, 1952.

Served: Nov. 3, 1952.

In the United States Court of Appeals
for the Ninth Circuit

T. C. Docket No. 24081

COMMISSIONER OF INTERNAL REVENUE,
Petitioner on Review,

vs.

ROY EATON,
Respondent on Review.

PETITION FOR REVIEW

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States in this proceeding on October 31, 1952, "That there is a deficiency in income and victory tax for the taxable year 1943 in the amount of $4.93, and that there are no deficiencies in income tax for the taxable years 1944, 1945, and 1946." This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The respondent on review, Roy Eaton, is an individual, whose mailing address is Route No. 1, Box 303, Fullerton, California, and who was, during the taxable years herein involved, a resident of the Territory of Hawaii or Fullerton, California. The said taxpayer filed his Federal income tax returns for the calendar years 1943, 1944, 1945 and 1946,

the taxable years here involved, with the Collector of Internal Revenue for the District of Hawaii.

Nature of Controversy

The sole question which was presented to and passed upon by The Tax Court of the United States is whether the income of a partnership in which the settlor-taxpayer was a general partner, and a trust created for the benefit of the taxpayer's three minor children was designated as a special partner, was taxable to the taxpayer, insofar as the share thereof allocable to the trust was concerned, under the doctrine of Helvering v. Clifford (1940), 309 U. S. 331.

In 1940 the taxpayer acquired franchises from Nehi Corporation to manufacture and sell Nehi beverages in the Hawaiian Islands. On September 30, 1942, a special was organized in which the taxpayer, Charles P. Johnson, and Walter L. Prock, Jr., were the general partners, and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, was the special partner. On the same date, September 30, 1942, the taxpayer executed a deed of trust for the benefit of his minor children, naming the Bishop Trust Company, Limited, as trustee, to which trust he paid the sum of $15,000 which it was required be contributed to the capital of the partnership for a 30 per cent interest therein. The taxpayer then conveyed to the partnership the assets used in his bottling business and the partnership assumed his liabilities in connection therewith. Beverage franchises were issued by the Nehi Cor-

poration on October 6, 1942, to the three general partners.

On February 28, 1943, a new trust was created by the taxpayer, for the benefit of his children, with the Bishop Trust Company, Limited, designated as trustee. All of the trust income was to be accumulated during the existence of the trust. The new trust became a special partner in the partnership.

In his notice of deficiency, the Commissioner held that the income of the Nehi Beverage Company of Hawaii which had been reported on fiduciary returns filed by the Roy Eaton Trust No. 2, as well as the income of the Roy Eaton Trust No. 1, was taxable to the taxpayer, Roy Eaton. The Tax Court of the United States disagreed with the Commissioner's determination and held that the settlor did not have sufficient control over the trusts to make the income thereof taxable to him, that the trusts were bona fide partners in the partnership and that their distributive shares of partnership income did not constitute income of the taxpayer.

/s/ CHARLES S. LYON,
Assistant Attorney General.

/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Recieved and filed January 19, 1953, T.C.U.S.

[Title of Court of Appeals and Cause.]

T. C. Docket No. 24082

PETITION FOR REVIEW

To the Honorable Judges of the United States Court of Appeals for the Ninth Circuit:

The Commissioner of Internal Revenue hereby petitions the United States Court of Appeals for the Ninth Circuit to review the decision entered by The Tax Court of the United States in this proceeding on October 31, 1952, "That there are no deficiencies or overpayments due in income tax for the taxable years 1945 and 1946." This petition for review is filed pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

The respondent on review, Genevieve H. Eaton, is an individual, whose mailing address is Route No. 1, Box 303, Fullerton, California, and who was, during the taxable years here involved, a resident of the Territory of Hawaii or Fullerton, California. The said taxpayer filed her Federal income tax returns for the calendar years 1945 and 1946, the taxable years here involved, with the Collector of Internal Revenue for the District of Hawaii.

Nature of Controversy

The sole question which was presented to and passed upon by The Tax Court of the United States is whether the income of a partnership in which the taxpayer's husband, Roy Eaton, was a general partner, and a trust created by him for the benefit

of the taxpayers' three minor children was designated as a special partner, was taxable to the taxpayer and her husband, on a community property basis, insofar as the share thereof allocable to the trust was concerned, under the doctrine of Helvering v. Clifford (1940), 309 U. S. 331.

In 1940 the taxpayer's husband, Roy Eaton, acquired franchises from Nehi Corporation to manufacture and sell Nehi beverages in the Hawaiian Islands. On September 30, 1942, a special partnership was organized in which Roy Eaton, Charles P. Johnson, and Walter L. Prock, Jr., were the general partners, and Bishop Trust Company, Limited, Trustee under Deed of Trust of Roy Eaton, was the special partner. On the same date, September 30, 1942, the taxpayer's husband executed a deed of trust for the benefit of their minor children, naming the Bishop Trust Company, Limited, as trustee, to which trust he paid the sum of $15,000 which it was required be contributed to the capital of the partnership for a 30 per cent interest therein. The taxpayer's husband then conveyed to the partnership the assets used in his bottling business and the partnership assumed his liabilities in connection therewith. Beverage franchises were issued by the Nehi Corporation on October 6, 1942, to the three general partners.

On February 28, 1943, a new trust was created by the taxpayer's husband, for the benefit of their children, with the Bishop Trust Company, Limited, designated as trustee. All of the trust income was to be accumulated during the existence of the trust.

The new trust became a special partner in the partnership.

In his notice of deficiency, the Commissioner held that the income of the Nehi Beverage Company of Hawaii which had been reported on fiduciary returns filed by the Roy Eaton Trust No. 2, as well as the income of the Roy Eaton Trust No. 1, was taxable to the taxpayer's husband, Roy Eaton, one-half of which income was included in the taxpayer's taxable income as her community share thereof. The Tax Court of the United States disagreed with the Commissioner's determination and held that the settlor did not have sufficient control over the trusts to make the income thereof taxable to him, that the trusts were bona fide partners in the partnership and that their distributive shares of partnership income did not constitute income of the taxpayer's husband.

/s/ CHARLES S. LYON,
Assistant Attorney General;

/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Received and filed January 19, 1953, T.C.U.S.

[Title of Court of Appeals and Cause.]

T. C. Docket No. 24081

STATEMENT OF POINTS

Comes Now the Commissioner of Internal Revenue, petitioner on review in the above-entitled cause, by his attorneys, H. Brian Holland, Assistant Attorney General, and Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and hereby states that he intends to rely upon the following points in this proceeding:

The Tax Court of the United States erred:

1. In entering its decision, "That there is a deficiency in income and victory tax for the taxable year 1943 in the amount of $4.93, and that there are no deficiencies in income tax for the taxable years 1944, 1945 and 1946."

2. In failing and refusing to sustain the deficiencies in tax determined by the Commissioner.

3. In holding and deciding that the trusts created by the taxpayer for the benefit of his minor children were bona fide partners in the partnership involved and that their distributive shares of partnership profits were not income of the taxpayer herein.

4. In failing and refusing to hold and decide that the trusts created by the taxpayer for the benefit of his minor children were not, for Federal income tax purposes, recognizable partners in the taxpayer's business known as Nehi Beverage Company of Hawaii.

5. In holding and deciding that the settlor-taxpayer did not have any rights in the trust corpora or income sufficient to make the income of the trusts taxable to him.

6. In failing and refusing to hold and decide that, under the doctrine of Helvering v. Clifford, 309 U. S. 331, the income of the trusts created by the settlor-taxpayer for the alleged benefit of his minor children was taxable to him.

7. In that its ultimate conclusion that the trusts created for the taxpayer's minor children were bona fide trusts created for the benefit of the said children and that the taxpayer did not have any substantial control over, or interest in, the corpora or the income of the trusts is not supported by but is contrary to its underlying findings of fact.

8. In that its opinion and its decision are not supported by but are contrary to the Court's findings of fact.

9. In that its opinion and its decision are not supported by but are contrary to the evidence.

10. In that its opinion and its decision are contrary to law and the Commissioner's regulations.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General;

/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Statement of Service:

A copy of this Statement of Points was mailed to Milton Cades, Esquire, 400 Bishop Trust Building, Honolulu, T. H., attorney for respondent on review, on April 2, 1953.

/s/ CHAS. E. LOWREY,
Special Attorney, Bureau of
Internal Revenue.

Filed April 2, 1953, T.C.U.S.

[Title of Court of Appeals and Cause.]

T. C. Docket No. 24082

STATEMENT OF POINTS

Comes Now the Commissioner of Internal Revenue, petitioner on review in the above-entitled cause, by his attorneys, H. Brian Holland Assistant Attorney General, and Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and hereby states that he intends to rely upon the following points in this proceeding:

The Tax Court of the United States erred:

1. In entering its decision, "That there are no deficiencies or overpayments due in income tax for the taxable years 1945 and 1946."

2. In failing and refusing to sustain the deficiencies in tax determined by the Commissioner.

3. In holding and deciding that the trusts created

by the taxpayer's husband, Roy Eaton, for the benefit of their minor children were bona fide partners in the partnership involved and that their distributive shares of partnership profits were not income of the taxpayers herein.

4. In failing and refusing to hold and decide that the trusts created by the taxpayer's husband, Roy Eaton, for the benefit of their minor children were not, for Federal income tax purposes, recognizable partners in his business known as Nehi Beverage Company of Hawaii.

5. In holding and deciding that the taxpayer's husband, Roy Eaton, did not have any rights in the corpora or income of the trusts created by him for the benefit of their minor children sufficient to make the income of the trusts taxable to him.

6. In failing and refusing to hold and decide that, under the doctrine of Helvering v. Clifford, 309 U. S. 331, the income of the trusts created by the taxpayer's husband, Roy Eaton, for the alleged benefit of their minor children was taxable to him and that the taxpayer was taxable on her community share of such income.

7. In that its ultimate conclusion that the trusts created by the taxpayer's husband, Roy Eaton, for their minor children were bona fide trusts created for the benefit of the said children and that he did not have any substantial control over, or interest in, the corpora or the income of the trusts is not supported by but is contrary to its underlying findings of fact.

8. In that its opinion and its decision are not supported by but are contrary to the Court's findings of fact.

/s/ CHAS. E. LOWREY,
Special Attorney, Bureau of

9. In that its opinion and its decision are not supported by but are contrary to the evidence.

10. In that its opinion and its decision are contrary to law and the Commissioner's regulations.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General;

/s/ CHARLES W. DAVIS,
Chief Counsel, Bureau of Internal Revenue, Attorneys for Petitioner on Review.

Statement of Service:

A copy of this Statement of Points was mailed to Milton Cades, Esquire, 400 Bishop Trust Building, Honolulu, T. H., attorney for respondent on review, on April 2, 1953.

Internal Revenue.

Filed April 2, 1953, T.C.U.S.

[Title Tax Court and Cause.]

Docket Nos. 24081 and 24082

CERTIFICATE OF CLERK

I, Ralph A. Starnes, Chief Deputy Clerk of The Tax Court of the United States, do hereby certify that the foregoing documents 1 to 43, inclusive, constitute and are all of the original papers and pro-

ceedings (including Original Exhibits 1 through 51, with the exception of # 30, not used, attached to the Stipulation of Facts; Petitioner's Exhibits 52 through 57, admitted in Evidence) on file in my office as the original and complete record in the proceedings before The Tax Court of the United States in the above-entitled proceedings and in which the Respondent in The Tax Court proceedings has initiated appeals as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceedings, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 10th day of April, 1953.

[Seal] /s/ RALPH A. STARNES,
Chief Deputy Clerk, The Tax Court of the United States.

No. 13806. United States Court of Appeals for the Ninth Circuit. Commissioner of Internal Revenue, Petitioner, vs. Roy Eaton, Respondent. Commissioner of Internal Revenue, Petitioner, vs. Genevieve H. Eaton, Respondent. Transcript of the Record. Petitions to Review a Decision of The Tax Court of the United States.

Filed April 13, 1953.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 13,806

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

ROY EATON and GENEVIEVE H. EATON,
Respondents.

PETITIONER'S DESIGNATION OF RECORD

The petitioner hereby designates for inclusion in the printed record on appeal the following portions of the typewritten record received by this Court from the Clerk of The Tax Court of the United States in the above-entitled cause:

1. Docket Entries, No. 24,081.
2. Docket Entries, No. 24,082.
3. Petition (with exhibit), No. 24,081.
4. Answer, No. 24,081.
5. Petition (with exhibit), No. 24,082.
6. Answer, No. 24,082.
7. Stipulation of Facts, with Exhibits 1 through 22, 29, and 31 through 36.
8. Transcript of Proceedings, 6-18-51, pp. 1, 24 through 102.
9. Findings of Fact and Opinion.
10. Decision, No. 24,081.
11. Decision, No. 24,082.
12. Petition for Review. No. 24,081.

13. Petition for Review, No. 24082.
14. Statement of Points, No. 24,081.
15. Statement of Points, No. 24,082.
16. This Designation.

Dated: April 28, 1953.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
Attorney for Petitioner.

[Endorsed]: Docketed and Filed April 30, 1953.